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**ROUTE1 INC.**

**MANAGEMENT DISCUSSION AND ANALYSIS**

**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2010**

**As at November 18, 2010**

The following discussion and analysis of the financial condition and results of operations (“**MD&A**”) of Route1 Inc. (also referred to as “**we**”, “**us**”, “**our**”, “**Route1**”, or the “**Company**”), has been prepared in accordance with National Instrument 51-102F1, reviewed and approved by the Company’s Board of Directors prior to filing and should be read in conjunction with the Company’s unaudited consolidated financial statements and related notes as at and for the three and nine months ended September 30, 2010, and the audited financial statements as at and for the year ended December 31, 2009, which have been prepared in accordance with Canadian Generally Accepted Accounting Principles (“**GAAP**”).

**FORWARD-LOOKING STATEMENTS**

The following discussion may contain forward-looking statements about matters that involve risk and uncertainties, such as statements of Route1’s plans, objectives, expectations and intentions, as well as financial trends. The discussion also includes cautionary statements about these matters. You should read the cautionary statements made below as being applicable to all forward-looking statements wherever they appear in this document. In drawing a conclusion or making a forecast or projection set out in the forward-looking information, the Company takes into account the following material factors and assumptions in addition to the above factors: the Company’s ability to execute on its business plan; the acceptance of the Company’s devices and services by its customers; the timing of execution of outstanding or potential customer orders by the Company; the sales opportunities available to the Company; the Company’s subjective assessment of the likelihood of success of a sales lead or opportunity; the Company’s historic ability to generate sales leads or opportunities; and that sales will be completed at or above the Company’s estimated margins. This list is not exhaustive of the factors that may affect our forward-looking information. These and other factors should be considered carefully and readers should not place undue reliance on such forward-looking information.

Factors that could cause Route1’s actual results to differ materially from the forward-looking statements are contained herein and include, but are not limited to, overall economic conditions, competitive pressures and unexpected technology changes. Additional information concerning risks and uncertainties affecting Route1’s business and other factors that could cause financial results to fluctuate is set forth later in this document, as well as elsewhere herein, and is contained in Route1’s filing with Canadian securities regulatory authorities, available on the SEDAR website ([www.sedar.com](http://www.sedar.com)) under Route1 Inc. and on the Company’s website ([www.route1.com](http://www.route1.com)).

This MD&A includes additional disclosures on the critical accounting policies and estimates, additional disclosure on the annual selected financial information, additional discussion and analysis on the factors affecting the Company’s financial performance, additional disclosure on future liquidity and capital needs including the addition of a tabular presentation of contractual obligation, additional disclosure on the last eight quarters, and details of related party

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transactions. The Company does not believe that any of the additional information provided, and that has not been otherwise disclosed in other filings, is material in nature.

## OVERVIEW

Route1 delivers industry-leading security and identity management solutions to corporations and government agencies who need universal, secure access to all digital resources and sensitive data. These customers depend on The Power of MobiNET<sup>®</sup> - Route1's communications and service delivery platform. MobiNET<sup>®</sup> provides identity assurance and individualized access to networks and data. Route1's patented solutions are based on FIPS-140-2 cryptographic modules, and simplify the process of meeting increasingly stringent regulatory requirements for privacy and security.

## HIGHLIGHTS

- On January 11, 2010, the Company announced that a U.S. based provider of telecommunications and data communications products, services, systems and solutions for the U.S. Federal government (the "Reseller") informed Route1 that it would not be respecting its contractual obligations under its agreement. The Reseller also informed the Company that it wished to continue to market and sell Route1 security and identity management solutions to the U.S. Federal Government in 2010, but on a non-exclusive basis. Route1 has communicated to the Reseller that it will continue to fulfill its obligations under the agreement and work with the Reseller to continue to service the U.S. Federal Government through the end of the agreement's term. The Company also informed the Reseller that in no way should the Company's actions be construed as a waiver of any of its rights under the agreement based on the Reseller's action to not respect certain material contractual obligations.
- On February 26, 2010, the Company announced the appointment of Tony P. Busseri as President and Chief Executive Officer of Route1. The Company also announced that Mr. White has stepped down as President and CEO of Route1 and will become Vice Chairman where he will continue to play an active role in business development.
- On February 26, 2010, the Company announced the closing of a non-brokered private placement of 38,000,000 units (Units) at \$0.05 per Unit (the Unit Price) for aggregate proceeds of CDN\$1,900,000 (the Offering) to Route1. Each Unit is comprised of one common share and one common share purchase warrant of Route1 (a Warrant). Each Warrant entitles the holder to purchase one additional common share of the Company at a price of \$0.15 per common share for a period of 60 months (the Expiry Date) following the closing date. Proceeds of the Offering will be used for general working capital and corporate purposes. No fees or commissions were paid as part of the Offering.
- On March 1, 2010, the Company announced that, as part of its management changes and compensation review, a total of 9,500,000 stock options were granted to an officer and a consultant of Route1. 5,250,000 of the stock options are exercisable at \$0.10 per share and the remaining 4,250,000 stock options are exercisable at \$0.15 per share.

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- On March 2, 2010, the Company announced the commercial availability of the MobiKEY Fusion™ device. The MobiKEY Fusion™ device extends portable and high assurance identity-based access to information and systems needed from anywhere, at any time, to identity and access cards based on the ID-1 standard. ID-1 is an international standard (ISO/IEC 7810-2003) commonly used for government-issued cards such as drivers' licenses and passports, bank cards, credit cards and other personal identity cards. The Route1 solution provides government and military users with a combination of ease-of-use and strong cryptography for in-theater operations. Coupled with strong multifactor identification and sophisticated entitlement controls, the MobiKEY Fusion™ device ensures that field personnel and warfighters have secure access to C4ISR (Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance) systems and information they need, when and where they need it.
  - On March 2, 2010, the Company announced that it has been selected to participate in a six-month pilot project to deploy the Route1 DEFIMNET® platform and the MobiKEY Fusion™ device to the U.S. Navy Reserve. Route1 is working with HP Enterprise Services to roll out the DEFIMNET® platform to a limited group of users in Navy Reserve Forces Command over the next six-months, which includes deploying and testing the DEFIMNET® platform. The objective of the pilot is to demonstrate increased flexibility for Navy personnel who require secure access to internal systems and digital resources when physical access to their normal working facilities and equipment is not practical. More than 300,000 potential DEFIMNET® platform users have been identified within the U.S. Navy. Personnel can connect to the DEFIMNET® platform using their MobiKEY Fusion™ devices that support the Department of Defence issued common access cards.
  - On March 24, 2010, the Company granted a total of 12,525,000 stock options to purchase common shares of Route1 to employees, officers and a director at an exercise price of \$0.13 per share, expiring on March 24, 2015.
  - On April 7, 2010 the Company announced that a total of 1,000,000 stock options were granted to a consultant of Route1. 500,000 of the stock options are exercisable at \$0.13 per share and 500,000 stock options are exercisable at \$0.15 per share. The grant is subject to regulatory approval. Under the Company's stock option plan, 10% of the issued capital or 38,838,811 common shares are reserved for issuance. Including the above grant, a total of 31,025,000 options are currently outstanding under the stock option plan.
  - On April 13, 2010, the Company announced the release of TruOFFICE® application software version 2.8 with strengthened security and Windows 7 support. This enables TruOFFICE® application software users the ability to connect to Microsoft® Windows 7 desktops from anywhere, at any time. This version also supports 64-bit Windows operating systems including 64-bit versions of Vista and Windows 7. In addition, TruOFFICE® application software version 2.8 now supports AES 256 (Advanced Encryption Standard) for encrypted data communications.
  - On April 28, 2010, the Company announced that the United States Patent and Trademark Office allowed Route1's patent application titled, "Portable Device for Accessing Host Computer via Remote Computer." Route1 expects its U.S. patent to be issued later this year. The Route1 patent application claims a portable device for enabling access to a host computer via a guest computer using an intermediary controller to set up the connection between the guest computer and the host computer. The guest computer interface may include a USB

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connector and a USB controller. The patent application expands on how the device may use a cryptographic processor to establish secure communication with the host computer. The portable device may be able to receive a biometric sample from a user, and allow the cryptographic processor to operate only when the biometric sample is for an authorized user.

- On May 10, 2010, the Company announced that a total of 32,360,333 warrants (the “Warrants”), issued as part of a private placement announced on October 15, 2007 (the “Offering”), expired on May 7, 2010, following an extension of the expiry date of the Warrants by six (6) months from November 7, 2009. The Warrants were issued with an exercise price of \$0.155 per share and had an original term of twenty-four (24) months.
- On May 12, 2010, the Company announced that The Fleet and Industrial Supply Center (FISC) Norfolk, Contracting Department, Philadelphia Office has procured directly from Route1, 400 MobiKEY Fusion™ devices and TruOFFICE® application software subscriptions on behalf of the Commander Navy Reserve Forces (RESFOR) in Norfolk, Virginia. The procurement was made in advance of completing the six-month pilot project to deploy the Route1 DEFIMNET® platform and MobiKEY Fusion™ devices to the U.S. Navy Reserve, which was announced on March 2, 2010.
- On May 19, 2010 and June 7, 2010, the Company granted a total of 325,000 and 4,000,000 stock options respectively to employees of Route1. 325,000 of the stock options are exercisable at \$0.13 per share, 2,000,000 of the stock options are exercisable at \$0.15 per share and 2,000,000 stock options are exercisable at \$0.20 per share. The grant is subject to regulatory approval. Under the Company’s stock option plan, 10% of the issued capital or 38,838,811 common shares are reserved for issuance. Including the above grant, a total of 35,350,000 options are currently outstanding under the stock option plan.
- On June 15, 2010, the Company announced that the United States Patent and Trademark Office has issued Route1’s first patent titled, “Portable Device for Accessing Host Computer via Remote Computer.” The abstract for U.S. Patent 7,739,726 B2, dated today, states:

A portable device enables access to a host computer via a guest computer. The portable device is connected to the guest computer, and a program stored in a memory on the portable device is activated, the program including instructions for establishing communication with the host computer such that input to the guest computer serves as input to the host computer, and output displays from the host computer are displayed on the guest computer. The portable device includes a cryptographic processor for performing cryptographic processing. The protected memory can be internal or external to the cryptographic processor. The Route1 MobiKEY® device is the portable device that is used to access a host computer from a remote computer. Route1 filed the patent on November 14, 2005.
- On June 23, 2010, the Company announced that it has fully repaid its non-revolving senior credit facility to its lender. The Company’s operating cash flow was used to make the payment.
- On July 15, 2010, the Company released a reports module for its MobiNET® administration and provisioning web-based portal (“MAP”). The MAP Reports Module allows administrators of MobiNET® services to configure and generate usage reports. Administrators are able to configure reports such as subscriber usage, detailed connection statistics for users and accounts, and account status. These reports should enable administrators to better manage their deployments and implement security policies around access rights to digital resources.

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- On July 26, 2010, the Company shipped to the Commander Navy Reserve Forces (RESFOR) in Norfolk, Virginia 400 MobiKEY Fusion™ devices and TruOFFICE® application software subscriptions. The procurement was made in advance of completing the six-month pilot project to deploy the Route1 DEFIMNET® platform and MobiKEY Fusion™ devices to the U.S. Navy Reserve, which was announced on March 2, 2010.
  - On August 24, 2010, the Company granted a total of 250,000 stock options to purchase common shares of Route1 to employees at an exercise price of \$0.15 per share, expiring on August 24, 2015.
  - On September 1, 2010, the Company announced that the United States Patent and Trademark Office has allowed Route1's patent application titled, "System and Method for Accessing Host Computer via Remote Computer."

The application claims a method of enabling communication between a host and a remote device using a controller, comprising connecting the controller to the host, connecting the controller to the remote device, the host and the remote device being in separate locations, validating, at the controller, digital identity certificates received from each of the host and the remote device, each identity certificate containing: (i) the public half of an asymmetric key algorithm key pair, (ii) identity information, and (iii) a digital signature of the issuing certificate authority, thereby converting the host to a validated host, and converting the remote device to a validated remote device, receiving, at the controller, a selection of the host from the validated remote device, sending parameters for the validated remote device from the controller to the selected host, sending an instruction, from the controller to the selected host, to establish a connection to the remote device, receiving, at the controller, notifications from the selected host and the validated remote device that a connection exists there between, and after receiving notice of a connection between the selected host and the validated remote device, refraining from involvement, at the controller, in transporting data between the selected host and the validated remote device, so that the selected host and the validated remote device subsequently communicate with each other without using any resource of the controller.

- On September 15, 2010, the Company announced that the following matters were voted on and approved at the Company's annual and special meeting of shareholders held on September 15, 2010: (1) Tony P. Busseri, Peter F. Chodos, Amar S. Doman, Michael F. Doolan and Michael D. Harris were elected as the Company's directors, and that Mr. Harris will continue as Chairman of the Board, (2) Deloitte & Touche LLP Chartered Accountants was reappointed as the Company's auditors in respect of the year ending December 31, 2010, and (3) the Company's stock option plan was reapproved. Each of the three matters that were voted on received greater than 97.4% approval. A total of 193.5 million shares were voted at the meeting.

Also, a total of 1,500,000 stock options were granted to Amar S. Doman on September 15, 2010 exercisable at \$0.20 per share.

- On September 16, 2010, the Company announced that the U.S. Government's Department of Homeland Security ("DHS") procured an additional 1,533 MobiKEY® devices and TruOFFICE® application software subscriptions through a reseller. Route1 fulfilled the order in September bringing DHS to 8,149 paid, active TruOFFICE® application software subscribers.

- On September 30, 2010, the Company announced the successful completion of the pilot project to deploy the Company’s DEFIMNET® platform, TruOFFICE® application software, and MobiKEY Fusion™ devices to the U.S. Navy Reserve Forces Command (“RESFOR”). The pilot successfully demonstrated increased flexibility for RESFOR personnel who require secure access to internal systems and digital resources when physical access to their normal working facilities and equipment is not possible or practical. There were multiple test scenarios including the ability to access the Navy Marine Corps Intranet (“NMCI”) systems and resources from multiple remote locations. Participants used their MobiKEY Fusion™ device from hotels, WIFI hotspots including at 37,000 feet on a commercial airliner, libraries, home and commercial networks.

The Navy’s Designated Accrediting Authority has completed its review of the DEFIMNET® platform and earlier in September 2010 provided an interim authority to test (“IATT”) for the DEFIMNET® platform. The DEFIMNET® platform has since then been connected to NMCI and a group of RESFOR participants have conducted the pilot project. The RESFOR pilot included the implementation, accreditation for IATT, and deployment on the NMCI network of Route1’s DEFIMNET® platform at a U.S. Navy Operations Center.

#### NON-GAAP FINANCIAL MEASURE: EBITDA

Within this MD&A we use the term EBITDA (earnings before interest, income taxes, depreciation and amortization, and restructuring and other costs). EBITDA does not have any standardized meaning prescribed under GAAP and is therefore unlikely to be comparable to similar measures presented by other companies.

We use EBITDA, among other measures, to assess the operating performance of our ongoing businesses without the effects of stock-based compensation and foreign exchange translation. We exclude stock-based compensation expense because it is largely dependent on the accounting methods and assumptions we use, along with non-operating factors, such as the value of our common shares. We exclude gains or losses on foreign exchange because they are generally not part of our ongoing operations.

EBITDA allows us to compare our operating performance over time on a consistent basis. We believe that certain investors and analysts use EBITDA to measure a company’s ability to service debt and to meet other payment obligations, or as a common valuation measurement in the technology industry.

Readers are cautioned that EBITDA should not be confused with cash flow from operating activities. The most comparable GAAP financial measure is *loss before undernoted*, which is discussed below. The table below reconciles EBITDA to *loss before undernoted* for the quarters presented.

<i>In thousands of Canadian dollars</i>	<b>Sept 30 2010</b>	June 30 2010	Mar 31 2010	Dec 31 2009	Sept 30 2009
EBITDA	<b>(284)</b>	(199)	(137)	(513)	(339)
Stock-based Compensation	<b>279</b>	223	65	27	70
Amortization	<b>23</b>	19	30	34	35
Loss before undernoted	<b>(586)</b>	(441)	(232)	(574)	(444)

## SELECTED FINANCIAL INFORMATION

The following table outlines selected unaudited financial information of the Company on a consolidated basis for the three and nine month periods ended September 30, 2010, 2009 and 2008.

<i>(in thousands of Canadian dollars, except per share amounts)</i>	As at and for the three months ended			As at and for the nine months ended		
	Sept 30, 2010	Sept 30, 2009	Sept 30, 2008	Sept 30, 2010	Sept 30, 2009	Sept 30, 2008
<b>STATEMENT OF OPERATIONS</b>						
<b>Revenue</b>						
Devices and appliances	\$ 386	\$ 703	\$ 287	\$ 644	\$ 1,822	\$ 419
Services	995	790	171	2,949	1,693	418
<b>Total Revenue</b>	<b>1,381</b>	<b>1,493</b>	<b>458</b>	<b>3,593</b>	<b>3,515</b>	<b>837</b>
Cost of revenue	350	477	286	595	1,482	637
<b>Gross margin</b>	<b>1,031</b>	<b>1,016</b>	<b>172</b>	<b>2,998</b>	<b>2,033</b>	<b>200</b>
<b>Operating expenses</b>						
General administration	610	507	658	1,664	1,333	2,037
Research and development	521	444	397	1,413	1,370	1,426
Selling and marketing	184	404	339	541	1,012	1,035
Stock-based compensation	279	70	56	567	189	273
Amortization	23	35	50	72	114	178
<b>Total operating expenses</b>	<b>1,617</b>	<b>1,460</b>	<b>1,500</b>	<b>4,257</b>	<b>4,018</b>	<b>4,949</b>
<b>Loss before undernoted</b>	<b>(586)</b>	<b>(444)</b>	<b>(1,328)</b>	<b>(1,259)</b>	<b>(1,985)</b>	<b>(4,749)</b>
Interest (expense) income	-	3	11	(16)	9	75
Foreign exchange translation	(12)	(137)	13	(113)	(166)	57
Proxy contest charges	-	(515)	-	-	(515)	-
Severance charges	(460)	-	-	(460)	-	-
<b>Net loss for the period</b>	<b>\$(1,058)</b>	<b>\$(1,093)</b>	<b>\$(1,304)</b>	<b>\$(1,848)</b>	<b>\$(2,657)</b>	<b>\$(4,617)</b>
<b>Loss per share</b>	<b>\$ (0.00)</b>	<b>\$ (0.00)</b>	<b>\$ (0.00)</b>	<b>\$ (0.00)</b>	<b>\$ (0.01)</b>	<b>\$ (0.01)</b>
<b>CASH FLOW INFORMATION</b>						
Operating activities	\$ (733)	\$(936)	\$(1,328)	\$ (1,517)	\$(1,803)	\$(4,638)
Investing activities	(57)	(4)	(3)	(3)	(10)	(96)
Financing activities	-	-	99	1,027	(3)	16
Net cash inflow (outflow)	(790)	(940)	(1,232)	(493)	(1,816)	(4,718)
Cash, beginning of period	937	1,244	2,817	640	2,120	6,303
<b>Cash, end of period</b>	<b>\$ 147</b>	<b>\$ 304</b>	<b>\$ 1,585</b>	<b>\$ 147</b>	<b>\$ 304</b>	<b>\$ 1,585</b>
Working capital (deficiency)	\$(887)	\$(624)	\$2,162	\$(887)	\$(624)	\$2,162
Total assets	\$2,437	\$3,526	\$4,382	\$2,437	\$3,526	\$4,382
Obligation under capital lease	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Shareholders' equity (deficiency)	\$(979)	\$(877)	\$2,403	\$(979)	\$(877)	\$2,403

## GOING CONCERN ASSUMPTION

Our consolidated financial statements have been prepared on a going concern basis, which assumes that the Company will be able to meet its commitments, realize its assets and discharge its liabilities in the normal course of business. For the three months ended September 30, 2010, the Company incurred a net loss of \$1,057,655. For the nine months ended September 30, 2010, the Company incurred a net loss of \$1,848,253, and had an accumulated deficit of \$36,057,132 and shareholders' deficiency of \$979,314 as at September 30, 2010. Continuation of the Company as a going concern is dependent upon achieving profitable operations, and the ability of the Company to obtain financing when necessary. If the going concern assumption were not appropriate for our consolidated financial statements, adjustments would be necessary in the carrying values of assets and liabilities, the reported net loss and the balance sheet classification used. Operating results for the current period are not necessarily indicative of the results to be expected for any future periods.

## COMPARISON FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009

### Revenue

Revenue for the three months ended September 30, 2010 was \$1,380,747, representing a decrease of \$112,010 or 7.5%, from \$1,492,757 for the same period in 2009. The comparison, discussed by segment, is as follows:

#### *Devices and Appliances*

Revenue from our device (the MobiKEY<sup>®</sup> device and the MobiKEY Fusion<sup>™</sup> device) and appliance segment (the DEFIMNET<sup>®</sup> platform and the EnterpriseLIVE AG appliance) for the three months ended September 30, 2010 was \$385,665, representing a decrease of \$317,403 or 45%, from \$703,068 for the same period in the 2009. Devices and appliances revenue as a percentage of total revenue represents 28% of total revenue for the three months ended September 30, 2010 as compared to 47% for the prior period. The reduction in devices and appliances revenue for the three months ended September 30, 2010 is a result of fewer device sales in the third quarter of 2010 versus the prior year (4,962 in 2009 versus 2,361 in 2010). The majority of device sales during the third quarter of 2009 were to the US and Dutch governments.

The table provided below details the number and sales value of MobiKEY<sup>®</sup> devices and MobiKEY Fusion<sup>™</sup> devices (collectively "MobiKEY Devices") sold during each of the last five quarters.

<b>MobiKEY Devices Sold</b> <i>(in thousands of Canadian dollars for Sales Value)</i>	<b>Sept 30</b> <b>2010</b>	<b>June 30</b> <b>2010</b>	<b>Mar 31</b> <b>2010</b>	<b>Dec 31</b> <b>2009</b>	<b>Sept 30</b> <b>2009</b>
Number	2,361	182	304	285	4,962
<b>Sales Value per Device</b>	<b>\$111</b>	<b>\$137</b>	<b>\$115</b>	<b>\$151</b>	<b>\$123</b>
Sales Value	\$263	\$25	\$35	\$43	\$610

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## Services

Revenue from our services segment (i.e. TruOFFICE<sup>®</sup> subscription-based services, and the DEFIMNET<sup>®</sup> platform and other appliance licensing or maintenance fees) for the three months ended September 30, 2010 was \$995,082, representing an increase of \$205,393 or 26%, from \$789,689 for the same period in 2009. Service revenue, as a percentage of total revenue, represents 72% for the three months ended September 30, 2010 as compared to 53% for the prior period. The increase in service revenue represents the continued growth in our TruOFFICE<sup>®</sup> application software subscriber base.

The table below provides information on the number of and revenue amount for the TruOFFICE<sup>®</sup> application software subscribers during each of the last five quarters.

<b>TruOFFICE<sup>®</sup> Subscribers</b> <i>(in thousands of Canadian dollars for Revenue)</i>	<b>Sept 30 2010</b>	<b>June 30 2010</b>	<b>Mar 31 2010</b>	<b>Dec 31 2009</b>	<b>Sept 30 2009</b>
Number	15,648	13,451	16,719	16,363	15,968
<b>Revenue per Subscriber</b>	<b>\$231</b>	<b>\$271</b>	<b>\$208</b>	<b>\$194</b>	<b>\$163</b>
Revenue	\$904	\$912	\$869	\$794	\$650

For the three months ended September 30, 2010, the subscriber number includes the 1,533 subscriptions sold to CBP on September 16, 2010. Revenue recognition for the new subscriber service, as per Company policy, will commence in the month of October 2010. Adjusting the subscriber base to 14,115 to reflect the paid subscribers for the quarter, the revenue per subscriber during the third quarter is \$256. The drop in revenue per subscriber from the second quarter is primarily related to foreign exchange.

During the second quarter ended June 30, 2010, current management evaluated the various pricing models which were used by the previous management team to arrive at a subscriber total. Current management, after reviewing the sustainable and upward trend seen on a revenue per subscriber basis, elected to terminate any heavily discounted and/or free subscriptions. All of these discounted and/or free service arrangements were with channel partners and had been put in place by past management.

The active subscriber number was adjusted in the second quarter of 2010 to reflect paid subscribers only and now stands at 15,648 as at September 30, 2010.

## Gross Margin

Gross margin is equivalent to revenue minus the cost of revenue. The cost of revenue primarily includes the cost of the devices and appliances sold, as well as the cost of their shipping and packaging, plus the cost to operate and maintain the MobiNET<sup>®</sup> platform.

The cost of revenue for the three months ended September 30, 2010 was \$349,467, representing a decrease of \$127,206 from \$476,673 for the same period in 2009. This decrease is primarily related to the decreased product costs associated with the decrease in sales of MobiKEY Devices incurred during the three months ended September 30, 2010.

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Gross margin for the three months ended September 30, 2010 was \$1,031,280 or 75% of gross revenue, representing an increase of \$15,196 from a gross margin of \$1,016,084 or 68% of gross revenue for the same period in 2009. The increase in gross margin can be largely attributed to a higher percentage of revenue derived from the service segment as our subscriber base is continuing to grow with the addition of new customers and users.

## **Expenses**

Operating expenses consist of general administration, research and development, selling and marketing, stock-based compensation and amortization. Operating expenses for the three months ended September 30, 2010 were \$1,616,928, representing an increase of \$157,230 or approximately 11%, from \$1,459,698 for the same period in 2009.

### *General administration*

General administration expenses consist primarily of salaries and benefits for administration staff, professional fees, rent, telephone, computer related expenses, directors' fees, insurance, bad debts, public company regulatory costs, and other indirect costs.

General administration expenses for the three months ended September 30, 2010 were \$609,912, representing an increase of \$103,480 or 20%, from \$506,432 for the same period in 2009 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses decreased by approximately \$75,000 for the three months ended September 30, 2010 as compared to the same period in 2009. For the three months ended September 30, 2009 there were one time payments of vacation pay and severance for the outgoing CEO and interim CEO;
- Legal and accounting fees increased by approximately \$25,000 for the three months ended September 30, 2010 as compared to the same period in 2009, as a result of additional patent, regulatory and legal matters during the current period;
- Professional fees increased by approximately \$74,000 from the same period in the prior year, as a result of additional director fees, management fees which includes consulting fees from the Company's President and CEO, and investor relations fees as a result of a new retainer fee structure; and
- Other overhead type expenses such as telephone, courier charges, equipment leasing, host facilities, insurance and computer related expenses increased by approximately \$70,000 for the three months ended September 30, 2010 as compared to the same period in 2009.

### *Research and development*

Research and development expenses consist of salaries and benefits for the research and development department, and other professional fees associated with development work.

Research and development expenses for the three months ended September 30, 2010 were \$521,567, representing an increase of \$77,283 or 17%, from \$444,284 for the same period in 2009 and the change can be summarized as follows:

- Salaries and benefits expenses increased by approximately \$66,000 for the three months ended September 30, 2010 as compared to the same period in 2009, as a result of more senior staffing in this department and payment of vacation to outgoing employees; and

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- For the three months ended September 30, 2010, the Company recorded an additional \$11,200 fee pertaining to the scientific research tax credits (“SRED”) for which the Company was entitled to in the 2009 tax year.

Research and development costs were also higher in the third quarter of 2010 in comparison to each of the two previous quarters in 2010 because the Company recorded a net tax credit of \$122,312 in Q2 2010 and a net tax credit of \$145,000 in Q1 2010.

#### *Selling and marketing*

Selling and marketing expenses consist primarily of salaries and commissions, agent fees, marketing and trade shows, and travel and entertainment.

Selling and marketing expenses for the three months ended September 30, 2010, were \$183,994, representing a decrease of \$219,529 or 54%, from \$403,523 for the same period in 2009 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses decreased by approximately \$82,000 for the three months ended September 30, 2010 as compared to the same period in 2009, primarily as a result of a reduction in head count compared to 2009;
- Sales commissions decreased by approximately \$74,000 for the three months ended September 30, 2010 as compared to the same period in 2009. This is mainly attributed to the commission expense the Company incurred last year for the sale of a DEFIMNET<sup>®</sup> platform; and
- An increase of approximately \$15,000 for travel costs associated with various meetings the Company attended in the United States as compared to the same period in 2009.

#### *Stock-based compensation*

Stock-based compensation was \$278,720 for the three months ended September 30, 2010, an increase of \$208,395 from \$70,325 for the same period in 2009. This increase is a result of the stock price in Q3 2010 being higher than in the same period a year earlier which resulted in adjustment to expenses for contractor issued options along with an increase in number of stock options granted during the current period.

#### *Amortization*

Amortization expense for the three months ended September 30, 2010 was \$22,735, representing a decrease of \$12,419 or 35% from \$35,154 for the same period in 2009. The decrease can be attributed to a net book value reduction in the asset base used in the calculation of amortization expense using the declining-balance method combined with minimal new capital expenditures in the quarter.

#### **Other Items**

##### *Interest (expense) income*

Interest expense for the three months ended September 30, 2010 was \$454, representing a decrease of \$3,291 from income of \$2,837 for the same period in 2009. Interest expense represents interest charges incurred by the Company for financing payment on the insurance of

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property and assets and is offset from interest income from cash balances the Company maintains in financial institutions. The cash balances for the three months ended September 30, 2010 were lower than for the same period in 2009.

#### *Foreign Exchange Translation*

Loss due to foreign exchange translation on balance sheet items such as Accounts Receivable, Accounts Payable and foreign bank accounts was a loss of \$11,553 for the three months ended September 30, 2010, an improvement of \$125,446 from a translation loss of \$137,446 for the same period in 2009.

#### *Severance Charges*

Severance charges for the three months ended September 30, 2010 were \$460,000 (2009- \$nil) and are a one-time expense the Company incurred to terminate the employment agreement of the Company's former President and CEO. The liability remaining as of September 30, 2010 has been recorded with both its short term (\$230,000) and long term components (\$210,833). Payment of this liability will be made over the coming 23 months, on a bi-monthly payment schedule and the liability will be fully discharged by August 31, 2012.

#### *Proxy Contest Charges*

Proxy contest charges for the three months ended September 30, 2010 were \$nil (2009- \$514,694). These charges represented legal fees, proxy solicitation fees and expenses, and other professional consulting fees related to the Annual and Special Shareholders Meeting held on September 24, 2009 which was a contested meeting. These charges were one time in nature and will not recur in the near future.

#### **Net loss**

Net loss for the three months ended September 30, 2010 was \$1,057,655 or \$0.00 per share, representing an improvement of \$35,262 from a net loss of \$1,092,917 or \$0.00 per share for the same period in 2009.

Net loss before interest expense, foreign exchange translation, severance charges and proxy contest charges for the three months ended September 30, 2010 was \$585,648 representing an increase of \$142,034 or 32% from a net loss of \$443,614 for the same period in 2009.

### **COMPARISON FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009**

#### **Revenue**

Revenue for the nine months ended September 30, 2010 was \$3,593,197, representing an increase of \$78,602 or 2%, from \$3,514,595 for the same period in 2009. The comparison discussed by segment is as follows:

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### *Devices and Appliances*

Revenue from our device (the MobiKEY<sup>®</sup> device and the MobiKEY Fusion™ device) and appliance segment (the DEFIMNET<sup>®</sup> platform and the EnterpriseLIVE AG appliance) for the nine months ended September 30, 2010 were \$644,111, representing a decrease of \$1,177,318 or 65%, from \$1,821,429 for the same period in the 2009. Devices and appliances revenue as a percentage of total revenue represents 18% of total revenue for the current period as compared to 52% for the prior period. The reduction in devices and appliances revenue for the nine months ended September 30, 2010, is due to 1) the sale of a DEFIMNET<sup>®</sup> platform in the second quarter of 2009 plus 2) a greater number of new MobiKEY Devices sold.

### *Services*

Revenue from our services segment (i.e. TruOFFICE<sup>®</sup> subscription-based services, and the DEFIMNET<sup>®</sup> platform and other appliance licensing or maintenance) for the nine months ended September 30, 2010, was \$2,949,086, representing an increase of \$1,255,920 or 74%, from \$1,693,166 for the same period in 2009. Service revenue, as a percentage of total revenue, represents 82% for the current period as compared to 48% for the prior period. The increase in service revenue represents the continued growth in our TruOFFICE<sup>®</sup> application software subscriber base.

Deferred revenue as at September 30, 2010 increased by \$630,485 to \$2,199,169 from \$1,568,684 as at December 31, 2009. This revenue will be recognized into income when such services are delivered and/or performed in future periods.

### **Gross Margin**

Gross margin is equivalent to revenue minus the cost of revenue. The cost of revenue primarily includes the cost of the devices and appliances sold, as well as the cost of their shipping and packaging, plus the cost to operate and maintain the MobiNET<sup>®</sup> platform.

The cost of revenue for the nine months ended September 30, 2010 was \$594,724, representing a decrease of \$886,825 from \$1,481,549 for the same period in 2009. This decrease is related to the cost of equipment sold as part of a DEFIMNET<sup>®</sup> platform transaction in the second quarter of the prior year and the increased product costs associated with the increase in sales of MobiKEY Devices incurred during the nine months ended September 30, 2009.

Gross margin for the nine months ended September 30, 2010 was \$2,998,473, representing an increase of \$965,427 from \$2,033,046 for the same period in 2009. This increase in gross margin can be largely attributed to a higher percentage of revenue derived from the service segment as our subscriber base continues to grow with the addition of new customers and users.

### **Expenses**

Operating expenses consist of general administration, research and development, selling and marketing, stock-based compensation and amortization. Operating expenses for the nine months ended September 30, 2010 were \$4,257,421, representing an increase of \$239,245 or approximately 6%, from \$4,018,176 for the same period in 2009.

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### *General administration*

General administration expenses consist primarily of salaries and benefits for administration staff, professional fees, rent, telephone, computer related expenses, directors' fees, insurance, bad debts, public company regulatory costs, and other indirect costs.

General administration expenses for the nine months ended September 30, 2010 were \$1,663,644, representing an increase of \$330,837 or 16%, from \$1,332,807 for the same period in 2009 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses decreased by approximately \$130,000 for the nine months ended September 30, 2010 as compared to the same period in 2009, primarily as a result of a reduction in head count compared to 2009. As well, in the prior year there were one time payments of vacation pay and severance for outgoing CEO and interim CEO;
- Professional fees increased by approximately \$350,000 from the same period in the prior year. This is primarily attributable to increased director fees of \$45,000, management fees, which, includes consulting fees from the Company's President and CEO of \$150,000, performance incentive payouts to two officers of the Company totaling \$55,000, and investor relations fees of \$36,000; and
- Other overhead type expenses such as telephone, courier charges, equipment rental, insurance and computer related expenses increased by approximately \$97,000 for the nine months ended September 30, 2010 as compared to the same period in 2009.

### *Research and development*

Research and development expenses consist of salaries and benefits for the research and development department, and other professional fees associated with development work.

Research and development expenses for the nine months ended September 30, 2010 were \$1,412,938, representing an increase of \$42,779 or 3%, from \$1,370,159 for the same period in 2009 and the change can be summarized as follows:

- Salaries and benefits expenses increased by approximately \$296,000 for the nine months ended September 30, 2010 as compared to the same period in 2009, as a result of an increase in head count in this department; and
- For the nine months ended September 30, 2010, the Company recorded a net tax credit of \$256,112 for scientific research tax credits ("SRED"). This credit represents the portion of SRED for which the Company was entitled to in the 2008 and 2009 taxation years.

### *Selling and marketing*

Selling and marketing expenses consist primarily of salaries and commissions, agent fees, marketing and trade shows, and travel and entertainment.

Selling and marketing expenses for the nine months ended September 30, 2010, were \$541,660, representing a decrease of \$470,255 or 46%, from \$1,011,915 for the same period in 2009 and the majority of the change can be summarized as follows:

- Salaries, benefits and commissions expenses decreased by approximately \$415,000 for the nine months ended September 30, 2010 as compared to the same period in 2009, primarily as

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a result of a reduction in head count compared to 2009 as well as savings due to commission cost the Company incurred for the sale of a DEFIMNET<sup>®</sup> platform last year; and

- Marketing costs, including travel expenses and tradeshow fees, decreased by approximately \$54,000 for the nine months ended September 30, 2010 as compared to the same period in 2009. This is mainly attributed to a decrease in trade show costs, which includes travel associated costs, as a result of the Company not attending as many events as compared to 2009.

#### *Stock-based compensation*

Stock-based compensation was \$567,545 for the nine months ended September 30, 2010, an increase of \$378,651 from \$188,894 for the same period in 2009. This increase is a result of the stock price being higher for the nine months ended September 30, 2010 than in the same period a year earlier which resulted in adjustment to expenses for contractor issued options along with an increase in stock options being granted during the current period.

#### *Amortization*

Amortization expense for the for the nine months ended September 30, 2010 was \$71,634, representing a decrease of \$42,767 or 37% from \$114,401 for the same period in 2009. The decrease can be attributed to a net book value reduction in the asset base used in the calculation of amortization expense using the declining-balance method combined with minimal new capital expenditures in the year.

#### **Other Items**

##### *Interest (expense) income*

Interest expense for the for the nine months ended September 30, 2010 was \$15,959, representing an increase of \$24,978 from interest income of \$9,019 for the same period in 2009. Interest expense represents interest charges incurred by the Company for financing payment on the insurance of property and assets as well as interest paid to a financial institution with respect to the credit facility that was in place earlier in the year. This is offset from interest income from cash balances the Company maintains in financial institutions. The cash balances for the nine months ended September 30, 2010 were lower than for the same period in 2009.

##### *Foreign Exchange Translation*

Loss due to foreign exchange translation on balance sheet items such as Accounts Receivable, Accounts Payable and foreign bank accounts was a loss of \$113,346 for the for the nine months ended September 30, 2010, a decrease of \$52,473 from a translation loss of \$165,819 for the same period in 2009.

##### *Severance Charges*

Severance charges for the three months ended September 30, 2010 were \$460,000 (2009- \$nil) and are a one-time expense the Company incurred to terminate the employment agreement of the Company's former President and CEO. The liability remaining as of September 30, 2010 has been recorded with both its short term (\$230,000) and long term components (\$210,833). Payment of this liability will be made over the coming 23 months, on a bi-monthly payment schedule and the liability will be fully discharged by August 31, 2012.

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### *Proxy Contest Charges*

Proxy contest charges for the nine months ended September 30, 2010 were \$nil (2009- \$514,694). These charges represented legal fees, proxy solicitation fees and expenses, and other professional consulting fees related to the Annual and Special Shareholders Meeting held on September 24, 2009 which was a contested meeting. These charges were one time in nature and will not recur in the near future.

### **Net loss**

Net loss for the nine months ended September 30, 2010 was \$1,848,253 or \$0.00 per share, representing an improvement of \$808,372 from a net loss of \$2,656,625 or \$0.00 per share for the same period in 2009.

Net loss before interest expense, foreign exchange translation, severance charges and proxy contest charges for the nine months ended September 30, 2010 was \$1,258,948 representing an improvement of \$726,182 or 36% from a net loss of \$1,985,130 for the same period in 2009.

### **SUMMARY OF QUARTERLY RESULTS**

The following table sets out selected unaudited financial information of the Company on a consolidated basis for the last eight quarters. The information has been derived from the Company's quarterly unaudited consolidated financial statements that, in management's opinion, have been prepared on a basis consistent with the consolidated annual financial statements and are reviewed and approved by the Company's Board of Directors. The Company's quarterly operating results have varied substantially in the past and may vary substantially in the future. Accordingly, the information below is not necessarily indicative of results for any future quarter.

As at and for the three months ended  
(in thousands of Canadian dollars, except per share data)

	Sept 30 2010	June 30 2010	Mar 31 2010	Dec 31 2009	Sept 30 2009	June 30 2009	Mar 31 2009	Dec 31 2008
<b>STATEMENT OF OPERATIONS</b>								
Revenue								
Devices and appliances	\$ 386	\$ 212	\$ 46	\$ 751	\$ 703	\$ 1,017	\$ 101	\$ 25
Services	995	995	959	944	790	566	338	307
Total revenue	1,381	1,207	1,005	1,695	1,493	1,583	439	332
Cost of revenue	350	138	107	288	477	896	109	164
Gross margin (loss)	1,031	1,069	898	1,407	1,016	687	330	168
Operating expenses								
General administration	610	641	413	989	506	340	487	483
Research and development	521	461	430	457	444	452	474	410
Selling and marketing	184	166	192	479	404	327	281	277
Stock-based compensation	279	223	65	27	70	68	51	18
Amortization	23	19	30	29	35	36	42	36
Total operating expenses	1,617	1,510	1,130	1,981	1,460	1,223	1,335	1,224
Loss before under noted	(586)	(441)	(232)	(574)	(444)	(536)	(1,005)	(1,056)
Interest (expense) income	-	(18)	2	3	3	3	3	6
Foreign exchange translation	(12)	(51)	(50)	(181)	(137)	(87)	58	220
Severance charges	(460)	-	-	-	-	-	-	-
Proxy contest	-	-	-	-	(515)	-	-	-
Net loss for the period	\$ (1,058)	\$ (510)	\$ (280)	\$ (752)	\$ (1,093)	\$ (620)	\$ (944)	\$ (830)
Loss per share	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)
<b>CASH FLOW INFORMATION</b>								
Operating activities	\$ (733)	\$ 373	\$ (1,155)	\$ (557)	\$ (935)	\$ 492	\$ (1,359)	\$ 548
Investing activities	(57)	63	(30)	41	(5)	(3)	(3)	(4)
Financing activities	-	(835)	1,881	852	-	-	(3)	(9)
Net cash inflow (outflow)	(790)	(399)	696	336	(940)	489	(1,365)	535
Cash, beginning of period	937	1,336	640	304	1,244	755	2,120	1,585
Cash, end of period	\$ 147	\$ 937	\$ 1,336	\$ 640	\$ 304	\$ 1,244	\$ 755	\$ 2,120
<b>BALANCE SHEET INFORMATION</b>								
Working capital (deficiency)	\$ (887)	\$ (392)	\$ 92	\$ (1,622)	\$ (624)	\$ 558	\$ 608	\$ 1,433
Total assets	\$ 2,437	\$ 2,753	\$ 3,481	\$ 2,041	\$ 3,526	\$ 2,784	\$ 2,865	\$ 4,221
Shareholders' equity (deficiency)	\$ (979)	\$ (200)	\$ 86	\$ (1,580)	\$ (877)	\$ 163	\$ 698	\$ 1,591

The Company's revenue and financial results are difficult to forecast and have historically fluctuated on a quarterly basis, and it is expected that quarterly revenue and financial results will continue to fluctuate in the future as the Company continues growing. Fluctuations in results are related to the growth of the Company's revenue, the timing of revenue being recognized and sales to customers, which may place large single orders in any one quarter, and the timing of staffing and infrastructure additions to support growth.

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## LIQUIDITY AND CAPITAL RESOURCES

Management continually assesses liquidity in terms of the ability to generate sufficient cash flow to fund the business. Net cash flow is affected by the following items: i) operating activities, including the level of accounts receivable, inventory, prepaid expenses, accounts payable and deferred revenue; ii) investing activities, including the purchase of capital assets; and iii) financing activities, including the issuance of capital stock.

### *Cash flow used in operating activities*

Cash flow used by operating activities (“OCF”) for the three months ended September 30, 2010 was \$756,200, compared to \$987,458 in the same period in 2009, representing an improvement of \$231,258. Non-cash working capital activities provided \$22,770 for the three months ended September 30, 2010 versus \$51,685 in the same period a year earlier. Therefore net cash used by the day-to-day operations for the three months ended September 30, 2010 was \$733,430 compared to \$935,773 in the same period in 2009, representing a decrease and improvement of \$202,343.

Cash flow used by operating activities (“OCF”) for the nine months ended September 30, 2010 was \$1,209,074, compared to \$2,353,330 in the same period in 2009, representing an improvement of \$1,144,256. Non-cash working capital activities used \$308,295 for the nine months ended September 30, 2010 versus providing non-cash working capital \$549,903 in the same period a year earlier. Therefore net cash used in the day-to-day operations for the nine months ended September 30, 2010, 2010 was \$1,517,369 compared to \$1,803,427 in the same period in 2009, representing a decrease and improvement of \$286,058.

### *Cash flow used in investing activities*

Cash flow used in investing activities for the three months ended September 30, 2010 was \$56,516 compared to \$4,529 in the same period in 2009, representing an increase in the outflow of cash of \$51,987. The increase can be attributed to an investment in capital assets by the Company in hardware equipment and software.

Cash flow used in investing activities for the nine months ended September 30, 2010 was \$2,760 compared to \$10,139 in the same period in 2009, representing a decrease in the outflow of cash of \$7,379. Investment by the Company in capital assets for the nine months ended September 30, 2010 was recovered by the collection of outstanding notes receivable during the year.

### *Cash flow provided by financing activities*

Cash inflow by financing activities for the three months ended September 30, 2010 and 2009 was \$nil.

Cash inflow by financing activities for the nine months ended September 30, 2010 was \$1,026,778 compared to cash outflow of \$2,700 for the same period in 2009, representing an increase in cash provided of \$1,029,478. This increase in cash is a direct result of the February 26, 2010 private placement, which provided gross proceeds of \$1,900,000 to the Company offset

by the repayment of the credit facility the Company had in place with a financial institution earlier in the year of approximately \$855,000.

The cash balance of the Company at September 30, 2010 was \$146,694, a decrease of \$493,351 from December 31, 2009. Current assets at September 30, 2010 were \$2,258,011 compared to \$1,965,987 at December 31, 2009. Working capital increased by \$735,011 to a deficiency of \$886,800 as of September 30, 2010 from a deficiency of \$1,621,811 in working capital as of December 31, 2009.

The Company had a \$1,000,000 (Dec. 31, 2009 - \$1,000,000) non-revolving senior credit facility that bore interest at bank prime plus 2.5% per annum. On June 23, 2010, the Company repaid the credit facility in full (Dec. 31, 2009 - \$854,717). The credit facility terminated on the repayment.

Interest expense related to this credit facility for the six months ended June 30, 2010 was \$18,591 (2009-\$nil).

The following table discloses future payments as at September 30, 2010 committed by the Company over the next five (5) years. It includes both principal and interest obligation's required under capital lease agreements and all other current contractual commitments.

Contractual Obligations	Payment Due by Period				
	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Severance liability	\$ 440,833	\$ 230,000	\$ 210,833	\$ -	\$ -
Operating leases	48,000	48,000	-	\$ -	\$ -
	\$ 488,833	\$ 278,000	\$ 210,833	\$ -	\$ -

## OFF-BALANCE SHEET ARRANGEMENTS

The Company has not entered into any off balance sheet arrangements.

## FUTURE INCOME TAXES

The Company follows the liability method of accounting for income taxes. Under this method future income tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Valuation allowances are established when necessary to reduce future income tax assets to the amount expected to be realized. As at September 30, 2010, we continue to carry a full valuation allowance against our income tax asset due to the uncertainty surrounding their full usage. There will be no income tax expenses against earnings in Canada until either all unrecognized operating loss carry-forwards of approximately \$36,302,000 are used or expire. The carry-forwards expire between 2010 and 2029.

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## TRANSACTIONS WITH RELATED PARTIES

The Company had the following transactions and/or outstanding amounts with related parties for the three and nine months ended September 30, 2010:

- Recorded interest income of \$nil for the three months ended September 30, 2010 and \$1,488 for the nine months ended September 30, 2010, related to \$85,000 advanced in terms of a promissory note dated January 8, 2008 to the former President and CEO of the Company bearing interest at 6% per annum. As at June 30, 2010, the total outstanding amount including interest was fully repaid to the Company.
- Recorded interest income of \$nil for the three months ended September 30, 2010 and \$1,000 for the nine months ended September 30, 2010, related to \$50,000 advance in terms of a promissory note dated December 28, 2007 to the Executive Vice-President and CTO of the Company, secured and due on demand bearing interest at 6% per annum. As at June 30, 2010 the total outstanding amount including interest was fully repaid to the Company.
- Recorded interest income of \$nil for the three months ended September 30, 2010 and \$556 for the nine months ended September 30, 2010, related to \$27,800 advance in terms of a promissory note dated June 17, 2005 to the Executive Vice-President and CTO of the Company, secured and due on demand bearing interest at 6% per annum. As at June 30, 2010 the total outstanding amount including interest was fully repaid to the Company.
- The Company made payments to 1220764 Ontario Inc. for management services provided by Mr. Tony P. Busseri, a director of the Company in the amount of \$60,000 for the three months ended September 30, 2010 and \$185,000 in the nine months ended September 30, 2010.

## PROPOSED TRANSACTIONS

The Company has not entered into any asset or business acquisition or disposition transactions.

## CRITICAL ACCOUNTING ESTIMATES

The Company's consolidated unaudited interim financial statements as at September 30, 2010 have been prepared in accordance with Canadian GAAP. Management makes certain estimates and relies on certain assumptions relating to reporting the Company's assets and liabilities as well as operating results in order to prepare the unaudited interim consolidated financial statements in conformity with Canadian GAAP. On an on-going basis, the Company evaluates its estimates and assumptions including those related to revenue, the valuation of accounts receivable, the estimation of useful lives of the various classes of capital assets, investments, stock-based compensation expense, and the measurement of income tax valuation allowances. Actual results could differ from those estimates, which are as follows:

- The Company's revenue is derived from hardware (i.e. the MobiKEY<sup>®</sup> device and the MobiKEY Fusion<sup>™</sup> device) sales and subscription services (i.e. TruOFFICE<sup>®</sup> application software). The Company recognizes revenue in accordance with EIC 141, "Revenue Recognition", and EIC 142, "Revenue Arrangements with Multiple Deliverables".

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- In the determination of the valuation of accounts receivable, including the allowance for doubtful accounts, the Company relies on current customer information, payment history and trends as well as future business and economic conditions.
  - The determination of inventory obsolescence allowance.
  - The determination of fair value of investments is based on a discounted cash flow model.
  - The estimation of useful lives of the various classes of capital assets is based upon history and experience of similar assets within each class.
  - The fair value of stock options is based on certain estimates applied to the Black-Scholes option-pricing model as disclosed in the Company's financial statements.
  - The measurement of the income tax valuation allowance is based upon estimates of future taxable income and the expected timing of reversals of temporary differences.

### **CHANGES IN ACCOUNTING POLICIES INCLUDING INITIAL ADOPTION**

There is no current period accounting policy changes.

### **RECENT ACCOUNTING PRONOUNCEMENTS ISSUED NOT YET ADOPTED**

#### *International Financial Reporting Standards*

On February 13, 2008, the Canadian Accounting Standards Board (“**AcSB**”) confirmed the mandatory International Financial Reporting Standards (“**IFRS**”) changeover date for Canadian profit-oriented publicly accountable entities (“**PAEs**”). This means that PAEs will be required to prepare financial statements in accordance with IFRS for interim and annual financial statements for fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require restatement for comparative purposes of amounts reported by the Company for annual and interim periods for the year ended December 31, 2010.

Canadian GAAP will be converged with IFRS through a combination of two methods: (1) as current joint-convergence projects of the United States Financial Accounting Standards Board and the International Accounting Standards Board are agreed upon, they will be adopted by the AcSB and may be introduced in Canada before the completed changeover to IFRS; and (2) standards not subject to a joint-convergence project will be exposed in an omnibus manner for introduction at the time of the complete changeover to IFRS.

As the International Accounting Standards Board currently, and expectedly, has projects underway that should result in new pronouncements that continue to evolve IFRS, the Canadian convergence initiative is evolving as it approaches implementation. The Company anticipates that it will not adopt IFRS for annual and interim reporting periods before the fiscal year beginning January 1, 2011.

The Company has completed an analysis of the impact of IFRS on accounting policies, information systems and internal controls over financial reporting. The analysis includes those policies the Company will be required to use, as well as those the Company would expect to apply where choices are permitted in preparing IFRS financial statements. To facilitate this transition in January 1, 2011, the Company will internally apply IFRS to the 2010 quarterly results, retroactively on December 31, 2010, ensuring that comparative results for fiscal year

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2010 will be available when preparing the 2011 financial reports. Changes implemented when converting to IFRS will be reported in 2010's fourth quarter MD&A.

The Company started its IFRS conversion process in 2009. It consisted of three primary phases as follows:

- 1) ***Scoping and diagnostic phase***  
This phase involved the establishment of a team leader on the project from the management team and then involved a high-level assessment to identify key areas that may be affected by the transition to IFRS, and ranking these as high, medium or low priority.
- 2) ***Impact analysis, evaluation and design phase***  
In this phase, each area identified from the scoping and diagnostic phase is being addressed by performing an in-depth analysis of Canadian GAAP/IFRS differences, evaluation and selection of available accounting policies, quantification of impacts and development of draft IFRS financial statement contents. This phase also includes the identification of operational impacts such as information technology, process and internal control changes.
- 3) ***Implementation and review phase***  
This phase involves the implementation of the necessary changes to the Company's information systems and business processes as identified through the assessment and design phases of the changeover plan. Significant implementation phase milestones will include the development of IFRS-compliant financial models, budgeting and reporting processes, the implementation of the Company's 2010 dual reporting systems strategy, the amendment and testing of internal controls over financial reporting and disclosure controls and procedures impacted by accounting policy changes, the implementation of internal and external communication plans, and the preparation of a January 1, 2010 opening balance sheet and 2010 comparative data under IFRS, with reconciliations from Canadian GAAP. The implementation phase will culminate in the preparation of Route1's financial reporting under IFRS beginning in 2011.

The Company completed the planning and scoping and diagnostic phase. The Company has drafted technical papers and is in the process of selecting accounting policies. The Company has identified the areas expected to have an impact on its financial statements and categorized them as High, Medium or Low impact. These areas do not represent a complete list of expected changes. As the Company progresses further into the implementation phase, and as changes to Canadian GAAP and IFRS standards may occur prior to its changeover date, the differences and impacts described below may be subject to change. The Company will continue to disclose additional impacts on its financial reporting, including expected quantitative impacts, systems and processes and other areas of business in future MD&As as they are determined. The Company anticipates having completed its IFRS conversion requirements by December 31, 2010.

### ***First time adoption***

The Company's adoption of IFRS will require the application of IFRS 1 First-time Adoption of International Financial Reporting Standards ("IFRS 1") which provides guidance for an entity's initial adoption of IFRS. IFRS 1 generally requires that an entity apply all IFRS effective at the

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end of its first IFRS reporting period retrospectively, with specific mandatory exemptions and a limited number of optional exemptions. Policy decisions with respect to applicable IFRS 1 choices are in the process of being documented for senior management to review and approve those choices. The following paragraphs outline some of the significant optional IFRS 1 exemptions the Company expects to apply in its first IFRS financial statements and the areas likely to have the highest impact on the Company's accounting policies.

The Company has identified that under *First time adoption* that it has options for 16 elective exemptions of which 9 do not apply to the Company and 4 mandatory exemptions of which 3 do not apply to the Company. Some of the available optional exemptions are as follows:

***Business Combinations (IFRS 3)***

IFRS allows an entity that has conducted prior business combinations to apply IFRS 3 on a prospective basis only from the date of transition or from another date selected by the Company. This avoids the requirement to restate prior business combinations.

The Company will elect to follow IFRS 3 from the time of transition of January 1, 2011. No impact on the financial statements is expected.

***Fair value or revaluation as deemed cost (IAS 16, 40 and 38)***

***Property, Plant and Equipment***

Consistent with Canadian GAAP, under IFRS, separable components of property, plant and equipment are recognized initially at cost. Under IFRS an entity is required to choose to account for each class of property, plant and equipment using either the cost model or the revaluation model. The cost model is generally consistent with Canadian GAAP where an item of property, plant and equipment is carried at its cost less any accumulated depreciation and any accumulated impairment losses. Under the revaluation method an item of property, plant and equipment is carried at its revalued amount, being its fair value at the date of the revaluation less any accumulated depreciation and accumulated impairment losses. Subsequent increases in fair value are recorded to the revaluation surplus account in equity while decreases in fair value serve to reduce the revaluation surplus account related to the asset, with any excess recognized in income. The Company has chosen not to fair value property, plant and equipment on transition.

No material impacts to recorded amounts are expected upon conversion to IFRS. The adjustment to financial statements will be as follows: 1) The zero net book value items will be eliminated from both the asset base and accumulated depreciation schedule; and 2) the Company's own-use of equipment will be categorized separately.

***Assets and liabilities of subsidiaries, associates, and joint venture (IAS 27, 28 and 31)***

Provides certain allowances and requirements for situations where the parent and its investees (subsidiaries, associates, and joint ventures or equity investments) adopt IFRS at different dates.

No impact on the financial statements is expected.

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***Designation of previously recognized financial instruments (IAS 39)***

Allows an entity to make an available-for-sale designation, or designate any financial asset or financial liability as at fair value through profit or loss at the date of transition.

No impact on the financial statements is expected.

***Share-based payment transactions (IFRS 2)***

Full retrospective application may be avoided for certain share-based instruments depending on the grant date, vesting terms and settlement of any related liabilities.

The Company is still assessing the impact on the financial statements.

***Leases (IAS 17 and IFRIC 4)***

Instead of full retrospective application of IFRIC 4, an entity may elect to apply the less onerous transitional provisions of IFRIC 4. Also if a first-time adopter made the same determination under Canadian GAAP as that required by IFRIC 4, the first time adopter need not assess that determination when it adopts IFRS.

The Company has determined that there is no impact on the financial statements.

***Borrowing costs (IAS 23)***

Allows an entity to apply the transitional provisions of IAS 23 in lieu of full retrospective application. The IAS 23 transitional provisions allow an entity to choose the date to apply capitalization of borrowing costs related to qualifying assets. The effective date in this instance is considered to be the later of January 1, 2009 and the date of transition.

The Company will elect to apply IAS 23 on a prospective basis from the date of transition.

The available Mandatory exemption is as follows:

***Estimates***

Requires estimates at the date of transition to be consistent with estimates made for the same date in accordance with the previous GAAP unless there is objective evidence that those estimates were in error. In short, this precludes the use of hindsight.

***Business combinations, consolidated financial statements and non-controlling interests***

In January 2009, the CICA issued the following new Handbook sections: Section 1582, Business Combinations, Section 1601, Consolidated Financial Statements and Section 1602, Non-Controlling Interests which replace Section 1581, Business Combinations and Section 1600, Consolidated Financial Statements. These new Sections will be applicable to financial statements relating to fiscal years beginning on or after January 1, 2011. Early adoption is permitted to the extent the three new Sections are adopted simultaneously. Together, the new Sections establish

standards for the accounting for a business combination, the preparation of consolidated financial statements and the accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. The Company is currently evaluating the impact of the adoption of these new Sections on its consolidated financial statements. The Company does not expect that the adoption of these new Sections will have a material impact on its consolidated financial statements

In December 2009, the CICA issued EIC 175, Multiple Deliverable Revenue Arrangements, replacing EIC 142, Revenue Arrangements with Multiple Deliverables. This abstract provides updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated and the consideration allocated; require, in situations where a vendor does not have vendor-specific objective evidence (VSOE) or third party evidence of selling price, that the entity allocate revenue in an arrangement using estimated selling prices of deliverables; eliminate the use of residual method and require an entity to allocate revenue using the relative selling price method; and require expanded qualitative and quantitative disclosures regarding significant judgments made in applying this guidance. This EIC is effective for future years beginning on or after January 1, 2011. The Company is currently evaluating the impact of the adoption of these new standards on its consolidated financial statements.

## FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### a) Establishing Fair Value

The carrying amount of financial instruments including cash, accounts receivable, other receivables, notes receivable and accounts payable and accrued liabilities approximates fair value because of the short-term nature of these instruments. The following table sets out the classification, carrying amount, and fair value of the Company's financial assets and liabilities as at September 30, 2010 and December 31, 2009:

	September 30, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
FINANCIAL ASSET				
Held for trading				
Cash (i)	\$ 146,694	\$ 146,694	\$ 640,045	\$ 640,045
Loans and receivables				
Accounts receivable (i)	\$ 1,076,392	\$ 1,076,392	\$ 88,583	\$ 88,583
Other receivables (i)	\$ 26,811	\$ 26,811	\$ 34,954	\$ 34,954
Notes receivable (i)	\$ nil-	\$ nil-	\$ 173,000	\$ 173,000
FINANCIAL LIABILITIES				
Other liabilities				
Accounts payable and accrued liabilities (i)	\$ 1,216,853	\$ 1,216,853	\$ 1,197,258	\$ 1,197,258
Bank Indebtedness	\$ nil	\$ nil	\$ 854,717	\$ 854,717

(i) The fair value of these instruments approximates their carrying amount due to their short-term nature.

b) Fair value hierarchy

Financial instruments recorded at fair value on the Consolidated Balance Sheet are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- a. Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- b. Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- c. Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The following table presents the financial instruments recorded at fair value in the Consolidated Balance Sheet, classified using the fair value hierarchy described above:

	Level 1	Level 2	Level 3	Total financial assets and financial liabilities at fair value
<b>Financial assets</b>				
Cash	\$ 146,694	\$ -	-	\$ 146,694
<b>Total financial assets</b>	<b>\$ 146,694</b>	<b>\$ -</b>	<b>-</b>	<b>\$ 146,694</b>
<b>Financial liabilities</b>				
<b>Total financial liabilities</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

During the year, there has been no significant transfer of amounts between Level 1 and Level 2.

The Company has exposure to credit risk, liquidity risk and market risk associated with its financial assets and liabilities. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board of Directors has established the Audit Committee which is responsible for monitoring the Company's compliance with risk management policies. The Audit Committee regularly reports to the Board of Directors on its activities.

The Company's risk management program seeks to minimize potential adverse effects on the Company's financial performance and ultimately shareholder value. The Company manages its risks and risk exposures through a system of internal controls and sound business practices.

The Company's financial instruments and the nature of the risks which they may be subject to are set out in the following table.

	<b>Risks</b>			
	<b>Credit</b>	<b>Liquidity</b>	<b>Foreign Exchange</b>	<b>Interest Rate</b>
Cash	Yes		Yes	Yes
Accounts receivable	Yes		Yes	
Other receivables	Yes			
Notes receivable	Yes			
Accounts payable and accrued liabilities		Yes	Yes	
Bank Indebtedness	Yes	Yes		Yes

(a) *Credit Risk*

Credit risk arises from cash held with banks and credit exposure to customers, including outstanding accounts receivable. The maximum exposure to credit risk is equal to the carrying value (net of allowances) of the financial assets. The objective of managing credit risk is to prevent losses on financial assets. The Company assesses the credit quality of counterparties, taking into account their financial position, past experience and other factors. During the three months ended September 30, 2010, the largest single customer represented approximately 47.2% (a reseller with more than one customer) of recorded revenue. For the nine months ended June 30, 2010, the largest single customer represented approximately 38.1 % (a reseller with more than one customer) of recorded revenue.

*Cash*

Cash consists of bank balances. Credit risk associated with cash is minimized substantially by ensuring that these financial assets are invested in debt instruments of highly rated financial institutions. At September 30, 2010, the Company had cash consisting of cash on hand and deposits with banks of \$146,694 (December 31, 2009 - \$640,045). During the nine months ended September 30, 2010, the Company did not hold any investments in asset-backed commercial paper.

*Accounts receivable*

Accounts receivable consists primarily of accounts receivable from invoicing of devices and services. The Company's credit risk arises from the possibility that a customer which owes the Company money is unable or unwilling to meet its obligations in accordance with the terms and conditions in the contracts with the Company, which would result in a financial loss for the Company. This risk is mitigated through established credit management techniques, including monitoring customer's creditworthiness, setting exposure limits and monitoring exposure against these customer credit limits.

The carrying amount of accounts receivable are reduced through the use of an allowance for doubtful accounts and the amount of the loss is recognized in the statement of operations. When a receivable balance is considered uncollectible, it is written off against the allowance for accounts receivable. Subsequent recoveries of amounts previously

written off reduce other expenses in the statement of operations. At September 30, 2010, the largest single customer represented approximately 45.3% of accounts receivable. Subsequent to September 30, 2010 the amount from the largest single customer was paid in full.

The following table outlines the details of the aging of the Company's receivables as at September 30, 2010 and December 31, 2009:

	September 30, 2010	December 31, 2009
Current	\$ 639,668	\$ 31,427
Past due		
1 – 60 days	436,724	47,873
Greater than 60 days	-	27,743
Less: Allowance for doubtful accounts	-	(18,460)
Total accounts receivable, net	<u>\$ 1,076,392</u>	<u>\$ 88,583</u>

The following table outlines the details of the Allowance for Doubtful Accounts of the Company's receivables as at September 30, 2010 and December 31, 2009:

	September 30, 2010	December 31, 2009
Opening balance in period	\$ (18,460)	\$ (99,672)
Collected in period	-	1,297
Increase in reserve in period	-	(2,769)
Write-off in period	18,460	82,684
Closing balance in period	<u>\$ -</u>	<u>\$ (18,460)</u>

*(b) Liquidity Risk*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's objective in managing liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements at any point in time. In order to meet its financial liabilities, the Company has recently relied on collecting its accounts receivable.

The Company's ability to manage its liquidity risk going forward will require some or all of the following: the ability to secure capital and/or credit facilities on reasonable terms in the current market place and its ability to generate positive cash flows from operations.

The following table details the Company's contractual maturities for its financial liabilities, including interest payments and operating lease commitments, as at September 30, 2010:

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>Total</u>
Accounts payable and accrued liabilities	\$ 833,520	\$ 230,000	\$ 153,333	\$ 1,216,853
Operating lease commitments	36,000	12,000	-	48,000
	<u>\$ 869,520</u>	<u>\$ 242,000</u>	<u>\$ 153,333</u>	<u>\$ 1,264,853</u>

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(c) *Market Risk*

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the fair value of recognized assets and liabilities or future cash flows or the Company's results of operation.

*Foreign exchange*

The functional currency of the parent company is Canadian dollars and the reporting currency is Canadian dollars. As at September 30, 2010, the Company had non-Canadian dollar net monetary liabilities of approximately US\$69,500 and €833 (December 31, 2009 - approximately US\$271,400 and €136,000). Any changes in the respective exchange rates as at September 30, 2009 would have resulted in an exchange gain or loss which would have been included in the determination of net income.

*Interest rate*

The Company has cash balances which are exposed to interest rate fluctuations. At September 30, 2010, cash totalled \$146,694 (2009 - \$640,045). An increase of 100 basis points in the market interest rate would have decreased the net loss by approximately \$1,467 (a 100 basis point decrease would have had an equal but opposite effect) for the three months ended September 30, 2010.

## **OTHER MD&A REQUIREMENTS**

*Disclosure of Outstanding Share Data*

As of the date of this document, the following was outstanding:

- 388,388,115 common shares issued and outstanding
- 38,000,000 common share purchase warrants ("Warrants") convertible into 38,000,000 common shares at an exercise price of \$0.15/share expiring on February 26, 2015
- 34,450,000 common share purchase options ("**Options**") convertible into 34,450,000 common shares issued under the Company's stock option plan
  - 6,500,000 Options issued on September 24, 2009 at \$0.10/share expiring September 24, 2014
  - 1,500,000 Options issued on October 13, 2009 at \$0.10/share expiring October 13, 2014
  - 5,250,000 Options issued on February 26, 2010 at \$0.10/share expiring on February 26, 2015
  - 4,250,000 Options issued on February 26, 2010 at \$0.15/share expiring on February 26, 2015
  - 12,525,000 Options issued on March 24, 2010 at \$0.13/share expiring on March 24, 2015
  - 500,000 Options issued on April 7, 2010 at \$0.13/share expiring April 7, 2015
  - 500,000 Options issued on April 7, 2010 at \$0.15/share expiring April 7, 2015
  - 325,000 Options issued on May 19, 2010 at \$0.13/share expiring May 19, 2015
  - 2,000,000 Options issued on June 7, 2010 at \$0.15/share expiring June 7, 2015
  - 2,000,000 Options issued on June 7, 2010 at \$0.20/share expiring June 7, 2015
  - 250,000 Options issued on August 24, 2010 at \$0.15/share expiring August 24, 2015

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- 1,500,000 Options issued on September 15, 2010 at \$0.20/share expiring September 15, 2015
  - 2,650,000 Options issued on February 26, 2010 at \$0.10/share expiring on February 26, 2015 were forfeited.

### *Risk Factors and Uncertainty*

Although management has a positive outlook for the Company and continually improves and adapts the Company's risk mitigation strategies, operating in the technology industry inherently involves a certain level of risk and uncertainty. In management's opinion, the following risk factors, among others, should be considered when evaluating the Company's business and its results of future operations:

- Management's ability to secure additional financing, if needed, on reasonable terms. Access to such financing at acceptable commercial terms will be dependent on the timing of recognition and receipt of cash from our current receivables and contracts, on our ability to demonstrate execution of our business strategy and the general condition of the credit and/or equity markets. Such additional financing may be dilutive in nature to existing shareholders.
- The Company's access to credit or capital could be further restricted by the ongoing current global financial crisis which has restricted credit availability worldwide and could also impact its ability to continue operations.
- The Company's expected revenue in the short-term is expected to partially arise from a US\$1.6 million renewal of a large number of TruOFFICE<sup>®</sup> application software subscriptions and a DEFIMNET<sup>®</sup> platform maintenance agreement with the US Government ("USG"). If the USG were to discontinue its relationship with the Company, such event may have a material adverse impact on the Company's financial results.
- The Company's ability to collect payment on a timely basis for services delivered may have a material adverse impact on the Company's liquidity position.
- There is no assurance that any forward-looking statement will materialize. Unless otherwise indicated, forward-looking statements describe expectations as of the date of this document.
- Route1 disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.
- Route1 had net working capital deficiency at September 30, 2010 of \$886,800, which may not be sufficient to support current operating levels and growth objectives for the current fiscal year;
- Third-party claims for infringement of intellectual property rights by Route1, and the outcome of any litigation with respect thereto, may harm the Company's competitive advantage in the secure remote access industry;
- Route1's ability to successfully obtain patent or other proprietary or statutory protection for its technologies and products, may harm the Company's competitive advantage in the secure remote access industry;
- Route1's ability to obtain rights to use certain software or components which are supplied by third parties, may not be sufficient to support future sales volumes;
- The ability to run efficient and uninterrupted operation of Route1's MobiNET<sup>®</sup> platform, which could impact on the credibility of the Company's product and services;
- Route1's ability to establish new, and to build on its existing customer base, could also slow the Company's continued growth;

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- The occurrence of a breach or perception of a breach of Route1's secure product and service offering, may impact on the credibility of the Company's product and services;
  - The inappropriate disclosure of confidential information of the Company may impact on the credibility of the Company's product and services;
  - Competition, both with existing providers as well as with any future providers entering the marketplace, within the secure remote access industry may hamper future sales growth;
  - Route1's reliance on its suppliers and the risk that suppliers will not be able to deliver required components on a timely basis, which may slow future sales growth;
  - Any future government(s) regulation of the secure remote access industry, including but not limited to restrictions on encryption of the MobiKEY<sup>®</sup> device and the MobiNET<sup>®</sup> platform may hamper future growth;
  - Any significant economic downturn, in geographic areas where Route1 engages in business activities, that may cause those government agencies to reduce discretionary budget spending in areas such as secure identity solutions.

#### *Audit Committee*

Two of the three members of the Audit Committee are independent and all meet the qualifications of a financial expert.

#### *Legal proceedings*

The Company filed a Statements of Claim against certain reseller customers relating to non-payment of invoices in January 2008. The reseller customers maintained that based on non-sanctioned verbal representations made to them by certain employees of the Company who are no longer employed with the Company; they were not obligated to make payment in accordance with the terms of the written binding purchase agreements. As reflected in the Statements of Claim, the reseller customers entered into binding written agreements with Route1 to purchase MobiKEY<sup>®</sup> devices that were delivered in 2007 for which revenue of approximately \$333,000 were recorded during 2007 on the strength of these agreements.

The Company reached a settlement with one of the reseller customers mutually waiving any Statements of Claim or Counterclaims that had been filed. The amount that the Company was seeking for non-payment of invoices was for approximately \$174,000 in revenue. The settlement involved the Company restocking a portion of the inventory for a restocking fee.

The Company also arrived at a mutual agreement with the other reseller to restock the inventory the Company previously claimed as owing in their legal claim. The claim against the reseller expired on May 20, 2010. The Company will not be pursuing further legal action against the reseller.

#### **SEGMENTED INFORMATION**

The Company is organized and managed as a single reportable business entity with two distinct revenue segments, being devices and appliances, and services. At September 30, 2010, the Company had \$2,199,169 (December 31, 2009 - \$1,568,684) in deferred revenue.

	For the three months ended		For the nine months ended	
	September 30		September 30	
	2010	2009	2010	2009
<b>Revenues</b>				
Devices	\$ 385,665	\$ 703,068	\$ 644,111	\$ 1,821,429
Services	995,082	789,689	2,949,086	1,693,166
	<b>\$ 1,380,747</b>	<b>\$ 1,492,757</b>	<b>\$ 3,593,197</b>	<b>\$ 3,514,595</b>

## SUBSEQUENT EVENTS

On October 4, 2010, the Company received a purchase order for the use and support of the Route1 DEFIMNET<sup>®</sup> platform that is connected to the Navy Marine Corps Intranet and for Route1's TruOFFICE<sup>®</sup> application software. The purchase order is for a minimum of one month and a maximum of six months, and is valued between US\$225,000 and US\$1.35 million. The purchase order permits the usage of the Company's DEFIMNET<sup>®</sup> platform and TruOFFICE<sup>®</sup> application software during the term of the purchase order and includes licensing to support of up to 2,500 concurrent users.

On October 5, 2010, the Company signed a Co-Venture Agreement with Fox Crypto B.V. of Delft, The Netherlands, ("Fox-IT") under which Fox-IT is granted the non-exclusive right to be the Company's independent information technology security solutions provider for the Netherlands and other countries in the European Union. The agreement's initial term is for a period of five years and will include i) Route1 to build a MobiNET<sup>®</sup> platform that will be installed within a Fox-IT high assurance data center, ii) Fox-IT to market and sell Route1's TruOFFICE<sup>®</sup> application software and MobiKEY<sup>®</sup> device as well as provide Tier 1 support services to end users and iii) revenue sharing between the Company and Fox-IT.

On October 5, 2010, the Company entered into a \$500,000 credit facility with a banking and financial services organization consisting of a revolving \$450,000 demand operating facility and a \$50,000 credit card limit. The credit facility will carry an interest rate equal to the lender's prime rate of interest plus 2.00%. The credit facility will be secured by the assets of the Company with access to the demand operating facility component based on the balance and term of the Company's trade accounts receivables outstanding plus its available cash. The Company is required to maintain a current ratio in excess of 0.75:1.0 while any portion of the demand facility is outstanding.

October 12, 2010, the Company was issued its second patent (filed by the Company on September 7, 2004) titled, "System and Method for Accessing Host Computer via Remote Computer" by the United States Patent and Trademark Office. The abstract for U.S. Patent 7,814,216 B2 states: "In a peer-to-peer fashion, various host computers communicate with various remote computers using the internet so that user inputs from the remote computers are transferred to the host computers as if the user inputs occurred locally, and information generated by the host computers is displayed on the remote computers. Thus, a remote computer is able to access all of the information and application programs on the host computer".

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*Additional Information*

Additional information about Route1 is available from Route1's website at [www.route1.com](http://www.route1.com), the SEDAR website at [www.sedar.com](http://www.sedar.com), or by request from Route1's head office at 155 University Avenue, Suite 1920, Toronto, Ontario, Canada M5H 3B7 (telephone 416-848-8391).