
ROUTE1 INC.**MANAGEMENT DISCUSSION AND ANALYSIS****FOR THE YEAR ENDED DECEMBER 31, 2009****AS AT APRIL 6, 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, been reviewed and approved by the Company’s Board of Directors prior to filing and should be read in conjunction with the Company’s audited consolidated financial statements and related notes 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) under Route1 Inc. and on the Company’s website (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 transactions. The Company does not believe that any of the additional information provided that has not otherwise been disclosed in other filings is material in nature.

OVERVIEW

Route1 delivers award-winning security and identity management solutions to customers worldwide. These solutions provide universal, secure access to all digital resources and sensitive data. At the heart of Route1's solutions is MobiNET®, a communications and service delivery platform focused on identity management and entitlement-based access to resources. Route1's patent-pending solutions are based on FIPS-140-2 cryptographic modules, and simplify the process of meeting increasingly stringent regulatory requirements around privacy and security.

HIGHLIGHTS

- In January 2009, the Company announced that it signed an agreement granting a U.S. based provider of telecommunications and data communications products, services, systems and solutions for the U.S. Federal government (the "Reseller") exclusive rights to resell Route1's security and identity management solutions to the U.S. Federal Government in 2009. As part of the agreement, the Reseller committed in 2009 to purchase a minimum of 30,000 Route1 MobiKEY® devices and 30,000 TruOFFICE™ one-year subscription-based services, which was valued at approximately US\$8.0 million to the Company. The potential recurring annual revenue stream to Route1 from these 30,000 TruOFFICE™ subscription-based services is estimated at US\$5.5 million. In addition to the purchase commitment, the Reseller agreed to provide advertising and marketing support to promote Route1's solutions to various U.S. Federal departments and agencies. The Reseller also agreed to provide network-hosting services to Route1 from their facilities. The Company started delivering on this agreement in the second quarter of 2009 with the shipment of approximately 2,000 MobiKEY® devices and 2,000 TruOFFICE™ subscriptions having an approximate value of US\$500,000.
- In April 2009, the Company announced the successful installation of its DEFIMNET™ (DEFense Identity Management NETwork), its military version of its service delivery platform for identity and entitlement management, at a United States Government's Department of Homeland Security ("DHS") site. DEFIMNET was developed and designed to reside within all levels of classified and unclassified networks, and to interact with other defense network systems. DEFIMNET™ is sanctioned for use by military units to command and control confidentiality, integrity and availability of secure and real-time data. This initial three (3) year agreement announced by the Company in October 2008 for the installation and maintenance of DEFIMNET™ is valued in excess of US\$2 million and is being delivered through the Reseller under the Washington Interagency Telecommunications System ("WITS") 2001 Crossover contract. Based on preliminary discussions and the leverage strength of DEFIMNET™, management expects that upon completion of the installation of DEFIMNET™, will see DHS's subscriber base for the Company's MobiKEY® devices and TruOFFICE™ subscription-based services to grow significantly over the next 12 to 18 months.
- On July 20, 2009, the Company announced that Mr. Dean Peloso, a member of Route1's then Board of Directors, would step in immediately on an interim basis to serve as President and Chief Executive Officer of the Company. The move followed the removal of Mr. K. Andrew White who previously served in this role.
- On July 27, 2009, the Company announced that it had been awarded a National Master Standing Offer ("NMSO") contract by Public Works and Government Services Canada ("PWGSC"). Under the NMSO, Canadian Government departments and agencies have been

pre-approved to purchase up to \$20 million of Route1 products and services over a three-year period. Route1 is now pre-approved to supply the Government of Canada a solution that will allow its employees to perform their job functions outside of the office without any risk of data leakage.

- On August 10, 2009, the Company announced the introduction of its beta version of the MobiKEY® Fusion, an identity validation device that supports government-issued identity and access cards, powered by MobiNET®. Route1 demonstrated the MobiKEY® Fusion at the U.S. General Services Administration's 2009 Network Services Conference in Chicago, Illinois held between August 10 to 13, 2009.
- On August 31, 2009, the Company announced that the Government of the Netherlands Ministry Foreign Affairs (the "Ministry") increased its deployment of Route1's TruOFFICE™ subscription-based service and MobiKEY® devices to enable secure interactions with their digital resources from anywhere, at any time. The Route1 solution has been deployed to both personnel at headquarters in The Hague, Netherlands, as well as personnel located at Dutch embassies abroad. The Ministry has piloted the use of the Route1 MobiKEY® devices within the organization over the last year. The spread of the H1N1 Swine Flu pandemic was a catalyst for the Ministry to accelerate their MobiKEY® deployments in order to prepare for the pandemic by enabling employees to continue their work from locations outside of the office. The importance of ensuring the continuity of critical processes triggered the Ministry to augment the application of Route1's solution, since it had been tested and proven to meet Ministry requirements.
- On September 24, 2009, the Company announced that the Concerned Shareholder's Nominees to the Board of Directors received shareholder support at the Company's Annual and Special Meeting of Shareholders. Approximately 66% (138 million) of the shares voted at the meeting supported the Concerned Shareholder's Nominees to the Board, while the nominees proposed by the Company received approximately 31% (65 million) of the votes, and approximately 3% (6 million) of the shares were withheld from voting. As a result of the shareholder vote, the Company's Board of Directors has consisted of Messrs. Tony P. Busseri, Peter F. Chodos, Michael F. Doolan, Michael D. Harris, and K. Andrew White since the date of the meeting, with Mr. Harris appointed as Chairman of the Board. Shareholders also established the number of directors at five. Following the meeting, the Company terminated the contract of Dean Peloso as interim President and CEO and replaced Mr. Peloso with Mr. White as the Company's Interim President and CEO. A Special Committee consisting of the independent directors undertook a review of the claims and allegations made by the prior Board.
- On September 25, 2009, the Company announced that on September 24, 2009 a total of 6,500,000 options to purchase common shares of the Company were granted to all the directors of the Company, except Mr. White, at an exercise price of \$0.10 per share and expiring on September 24, 2014. Including the above grant, a total of 21,572,876 options were outstanding under the stock option plan at that time. Ninety (90) days following the election of a new board of directors at the Company's Annual and Special Meeting of Shareholders held on September 24, 2009, 3,550,730 options to purchase common shares of the Company held by the outgoing board of directors will expire unless exercised. These have now expired.

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- On October 15, 2009, the Company announced that the TSX Venture Exchange approved an extension to the expiry date of 32,360,333 common share purchase warrants, priced at \$0.155, from November 7, 2009 to May 7, 2010.
 - On October 16, 2009, the Company closed a \$2.5 million senior debt financing with a major Canadian financial institution. The financing bears interest at the bank's prime rate plus two and a half percent (2.5%) for a rate of four and three quarter percent (4.75%) on the closing date, and is scheduled to be repaid by February 28, 2010. The funds from the financing were to be used to purchase additional inventory to fulfill future orders.
 - On October 28, 2009, the Company announced that the Special Committee, consisting of the independent directors, after reviewing the report of an independent third party (Stanley M. Beck, Q.C), cleared K. Andrew White with respect to the claims and allegations made by the prior Board. Mr. White was appointed as President and CEO of Route1. As well, the Company announced that it had terminated its relationships with Mr. Anthony Rzepka, Executive Vice-President, Chief Financial Officer and Treasurer and Mr. Timothy Hyland, Executive Vice-President and Chief Operating Officer.
 - On December 17, 2009, the Company came to a mutual agreement to settle litigation involving claims filed by the Company and a reseller against each other. Pursuant to the settlement, the Company would receive back into inventory 1,600 MobiKEY® and to a restocking fee which was paid by the reseller.
 - As of December 31, 2009, the Company had drawn \$854,717 on its debt facility with a financial institution for the purchase of 12,000 MobiKEY® devices.

SELECTED FINANCIAL INFORMATION

The following table sets out selected audited financial information of the Company on a consolidated basis for the last three years ended December 31, 2009, 2008 and 2007.

<i>(in thousands of Canadian dollars, except per share amounts)</i>	As at and for the years ended		
	Dec 31, 2009	Dec 31, 2008	Dec 31, 2007
STATEMENT OF OPERATIONS			
Revenues			
Devices	\$ 2,572	\$ 444	\$ 633
Services	2,637	725	374
Total revenues	5,209	1,169	1,007
Cost of revenues	1,793	801	1,294
Gross margin	3,416	368	(287)
Operating expenses			
General administration	2,417	2,519	2,207
Research and development	1,832	1,836	2,246
Selling and marketing	1,493	1,312	2,306
Stock-based compensation	210	291	101
Amortization	121	214	285
Total operating expenses	6,073	6,172	7,145
Loss before undernoted	(2,657)	(5,804)	(7,432)
Interest income	12	81	68
Foreign exchange translation	(249)	276	(25)
Write-down on investment	-	-	(75)
Proxy contest	(515)	-	-
Net loss for the period	\$ (3,409)	\$ (5,447)	\$ (7,464)
Loss per share	\$ (0.01)	\$ (0.02)	\$ (0.03)
CASH FLOW INFORMATION			
Operating activities	\$ (2,369)	\$ (4,089)	\$ (6,720)
Investing activities	891	(100)	(334)
Financing activities	(2)	6	11,871
Net cash inflow (outflow)	(1,480)	(4,183)	4,817
Cash, beginning of period	2,120	6,303	1,486
Cash, end of period	\$ 640	\$ 2,120	\$ 6,303
Working capital (deficiency)	\$ (1,622)	\$ 1,433	\$ 6,196
Total assets	\$ 2,041	\$ 4,221	\$ 8,325
Obligation under capital lease	\$ -	\$ 3	\$ 91
Shareholders' equity (deficiency)	\$ (1,580)	\$ 1,591	\$ 6,652

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 year ended December 31, 2009, the

Company incurred a net loss of \$3,408,902, and has an accumulated deficit of \$34,208,879 and shareholders' equity deficiency of \$1,580,101 as at December 31, 2009. 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 YEAR ENDED DECEMBER 31, 2009 TO 2008

Revenue

Revenues for the year ended December 31, 2009 were \$5,209,455, representing an increase of \$4,039,993 or 345%, from \$1,169,462 for the same period in 2008. The comparison discussed by segment is as follows:

Devices

Revenues from our device segment (i.e. MobiKEY®, DEFIMNET™ equipment, and EnterpriseLIVE AG) for the year ended December 31, 2009 were \$2,572,148, representing an increase of \$2,128,038 or 479%, from \$444,110 for the same period in the 2008. Device revenue as a percentage of total revenue represents 43% of total revenue for the current period as compared to 49% for the prior period. This is due to the hardware revenue for the DEFIMNET™ of \$1,162,948 and increased delivery of MobiKEY® devices in the current year as compared to the same period in 2008. A total of 8,829 MobiKEY® devices were delivered in 2009, primarily to the Reseller and European customers.

Services

Revenues from our services segment (i.e. TruOFFICE™ subscription-based services, DEFIMNET™ software licenses and maintenance, and MAP – MobiNET® Administration and Provisioning Portal) for the year ended December 31, 2009 were \$2,637,307, representing an increase of \$1,911,955 or 264%, from \$725,352 for the same period in 2008. Service revenue, as a percentage of total revenue, represents 51% for the current period as compared to 62% for the prior period. The increase in service revenues represents the continued growth in our subscriber base for MobiNET® subscription-based services with new subscribers added during the year, including the recording of the DEFIMNET™ subscriptions that started in 2009 which was not present in 2008.

Deferred revenue for the year ended December 31, 2009 decreased by \$138,309 to \$1,568,684 from \$1,706,993 as at December 31, 2008. 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 revenues minus the cost of revenues. The cost of revenues primarily includes the cost of the devices sold, as well as that of their shipping and packing, plus the cost to operate and maintain the MobiNET® (the Company's infrastructure for its software based subscriptions services).

The cost of revenues for the year ended December 31, 2009 was \$1,793,134, representing an increase of \$991,576 from \$801,558 for the same period in 2008. This is primarily related to the increased product costs associated with the increase in sales of MobiKEY® devices during the year.

Gross margin for the year ended December 31, 2009 was \$3,416,321, representing an increase of \$3,048,417 from a gross margin of \$367,904 for the same period in 2008. This increase in gross margin can be largely attributed to a higher percentage of revenues being derived from the service segment which results in higher margins than device segment, and also associated with the subscriber base continuing to grow in the period with the addition of new customers.

Operating Expenses

Operating expenses consist of general administration, research and development, selling and marketing, stock-based compensation and amortization. Operating expenses for the year ended December 31, 2009 were \$6,073,233, representing a decrease of \$98,629 or approximately 2%, from \$6,171,862 for the same period in 2008.

General administration

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

General administration expenses for the year ended December 31, 2009 were \$2,417,449, representing a decrease of \$101,314 or 4%, from \$2,518,763 for the same period in 2008 and can be summarized as follows:

- Legal and accounting fees decreased by approximately \$130,000 for the year ended December 31, 2009 as compared to the same period in 2008, as a result of fewer regulatory and legal matters during the current quarter;
- Professional fees, such as director fees, management fees, recruitment and consulting, increased by approximately \$89,000 for the year ended December 31, 2009 as compared to the same period in 2008 as a result of incurring management fees, increased fees for the new board and an increase in use of recruitment services;
- Salaries and benefits expenses increased by approximately \$21,000 for the year ended December 31, 2009 as compared to the same period in 2008, as a result of the absorption of the CFO severance of \$216,000, which was partially offset by a reduction in head count compared to 2008; and
- Other overhead expenses such as bad debts, telephone, courier charges, equipment leasing and computer related expenses decreased by approximately \$25,000 for the year ended December 31 2009 as compared to the same period in 2008.

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 year ended December 31, 2009 were \$1,831,780, remaining relatively flat for the same period in 2008:

- Salaries and benefits expenses increased by approximately \$52,000 for the year ended December 31, 2009 as compared to the same period in 2008, as a result of an increase in head count in this department. This was offset by a reduction in R&D expenses which were incurred in 2008 for certification and validation of the technology such as FIPS 140-2 Validation.

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 year ended December 31, 2009, were \$1,492,868, representing an increase of \$181,010 or 14%, from \$1,311,858 for the same period in 2008 and can be summarized as follows:

- Salaries and benefits and commissions expenses increased by approximately \$257,000 for the year ended December 31, 2009 as compared to the same period in 2008; this is attributed to an increased commission expense related to the sale of the DEFIMNET™ as well as the severance cost of a senior executive of \$360,000 which was incurred during the year; and
- Marketing costs, including travel expenses and tradeshow fees, decreased by approximately \$76,000 for the year ended December 31, 2009 as compared to the same period in 2008. This is mainly attributed to a decrease in trade show costs as a result of the Company not attending as many events in 2009 such as the RSA Conference as compared to 2008..

Stock-based compensation

Stock-based compensation was \$209,825 for the year ended December 31, 2009, a decrease of \$81,504 or 28% from \$291,329 for the same period in 2008. This decrease was a result of no expenses being booked in 2009 for the cancelled stock option grants. The aforementioned stock options were cancelled as the grants were not in compliance with the policies of the TSX Venture Exchange.

Amortization

Amortization expense for the year ended December 31, 2009 was \$121,311, representing a decrease of \$92,485 or 43% from \$213,796 for the same period in 2008. The decrease can be attributed to computer hardware assets fully amortized in 2008 and therefore no expense incurred in the current year, and an overall reduction in the asset base used in the calculation of amortization expense using the declining-balance method combined with no new capital expenditures in the quarter.

Interest income

Interest income for the year ended December 31, 2009 was \$12,229, representing a decrease of \$68,991 or 85% from \$81,220 for the same period in 2008. This decrease was primarily due to lower cash balances during the year as compared to the same period in 2008.

Foreign Exchange Translation

Loss due to foreign exchange translation on balance sheet on items such as Accounts Receivable, Accounts Payable and foreign bank accounts was \$249,525 for the year ended December 31, 2009, a decrease of \$525,582 from a translation gain of \$276,057 for the same period in 2008. The Canadian dollar appreciated against the Euro and the American dollar during 2009 resulting in foreign exchange translation loss on balance sheet accounts like cash and Accounts Receivables.

Proxy Contest Charges

Proxy contest charges for the year ended December 31, 2009 was \$514,694 and represents 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 are expected to be one time in nature and not to recur in the future.

Net loss

Net loss for the year ended December 31, 2009 was \$3,408,902 or a negative \$0.01 per share, representing a significant improvement of \$2,037,779 or 37%, from a net loss of \$5,446,681 or a negative \$0.02 per share for the same period in 2008.

Net loss before interest income, foreign exchange translation and proxy contest charges for the year ended December 31, 2009 was \$2,656,592 representing a significant improvement of \$3,092,036 or 54% from a net loss of \$5,748,628 for the same period in 2008.

COMPARISON FOR THE THREE MONTHS ENDED DECEMBER 31, 2009 TO 2008

Revenue

Revenues for the three months ended December 31, 2009 were \$1,694,860, representing an increase of \$1,362,707 or 410%, from \$332,153 for the same period in 2008, with the comparison discussed by segment below.

Devices

Revenues from our device (i.e. MobiKEY®, DEFIMNET™ equipment, and EnterpriseLIVE AG) segment for the three months ended December 31, 2009 were \$750,719, representing an increase of \$725,598 for the same period in the 2008. Device revenue as a percentage of total revenue represents 44% of total revenue for the current period as compared to 7% for the prior period. This is mostly due to the correction of a DEFIMNET™ hardware sale in the amount of \$566,448 recorded in the quarter which was previously incorrectly recorded, in the second quarter of 2009, as deferred revenue.

Services

Revenues from our services (i.e. TruOFFICE™ subscription-based services, DEFIMNET™ software licenses and maintenance, and MAP – MobiNET® Administration and Provisioning Portal) segment for the three months ended December 31, 2009 were \$944,141, representing an increase of \$636,785 or 207%, from \$307,032 for the same period in 2008. Service revenue as a percentage of total revenue represents 56% of total revenue for the current period as compared to 93% for the prior period. This increase in revenues represents the continued growth in our subscriber base for MobiNET® subscription-based services with new subscribers added during the year and also includes the recording of the DEFIMNET™ subscription licenses that started in the second quarter of 2009 which was not present in the same period in 2008.

Gross Margin

Gross margin is equivalent to revenues minus the cost of revenues. The cost of revenues primarily includes the cost of the devices sold, as well as that of their shipping and packing, plus the cost to operate and maintain the MobiNET® (the Company's infrastructure for its software based subscriptions services).

The cost of revenues for the three months ended December 31, 2009 was \$288,430, representing an increase of \$124,404 or 76% from \$164,026 for the same period in 2008. This is primarily due to the increase in sales of MobiKEY® devices for the period.

Gross margin for the three months ended December 31, 2009 was \$1,406,430, representing a significant improvement of \$1,238,303 from a gross margin of \$168,127 for the same period in 2008. This increase in gross margin can be largely attributed to the correction of recognizable revenue for DEFIMNET™ hardware of an additional \$566,488. Also, an increase in revenues being derived from the service segment which results in higher margins than the device segment, and also associated with the subscriber base continuing to grow in the period with addition of new customers.

Operating 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 December 31, 2009 were \$1,981,097, representing an increase of \$756,386 or 62%, from \$1,224,711 for the same period in 2008; the increase is discussed in detail below.

General administration

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

General administration expenses for the three months ended December 31, 2009 were \$988,525, representing an increase of \$504,973 or 104%, from \$483,552 for the same period in 2008 and can be summarized as follows:

- Legal and accounting fees increased by approximately \$161,000 for the three months ended December 31, 2009 as compared to the same period in 2008, due to more regulatory and legal

matters during the three month period, and primarily associated with review of licensing agreements currently in place;

- Salaries and benefits expense increased by approximately \$122,000 for the three months ended December 31, 2009 as compared to the same period in 2008, this was due to the absorption of the CFO severance cost of \$216,000, which was partially offset by a reduction in head count compared to 2008;
- Professional fees, such as director fees, recruitment and consulting, increased by approximately \$213,000 for the three months ended December 31, 2009 as compared to the same period in 2008, due to incurring management fees, increased fees for the new board and an increase in use of recruitment services; and
- Other overhead type expenses such as telephone, equipment leasing, postage and courier, and computer related expenses increased by approximately \$50,000 for the three months ended December 31, 2009 as compared to the same period in 2008 which was primarily due to the overall increase in exchange fees for filings and additional computer related expenses as compared to the same period 2008.

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 December 31, 2009 were \$457,400, representing an increase of \$47,355 or 12% from \$410,045 for the same period in 2008 and can all be attributed to:

- Salaries and benefits expenses increased by approximately \$39,000 for the three months ended December 31, 2009 as compared to the same period in 2008 as a result of additional head count in this period; and
- Consulting fees increased by approximately \$8,000 for the three months ended December 31, 2009 as compared to the same period in 2008, as a direct result of the Company providing a US based customer with access to a technical person..

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 December 31, 2009 were \$478,566, representing an increase of \$201,314 or 73%, from \$277,252 for the same period in 2008 and can be summarized as follows:

- Salaries and benefits expenses and commissions increased by approximately \$154,000 for the three months ended December 31, 2009 as compared to the same period in 2008, this is attributed to the absorption of a senior executive's severance of \$360,000 which was partially offset by a reduction in head count and commission expense compared to 2008; and
- Marketing costs, including travel and tradeshow fees increased by approximately \$47,000 for the three months ended December 31, 2009 as compared to the same period in 2008 and can be mainly attributed to the Company reversing a trade show expense in the fourth quarter of 2008 that was no longer to be incurred but was expensed in a prior quarter of 2008.

Stock-based compensation

Stock-base compensation was \$27,178 for the three months ended December 31, 2009, an increase of \$9,254 or 52% from \$17,924 for the same period in 2008. This increase was a result of new options granted for a consulting firm and new board of directors.

Amortization

Amortization expense for the three months ended December 31, 2009 was \$29,428, representing a decrease of \$6,510 or 18% from \$35,938 for the same period in 2008. The decrease can be attributed to computer hardware assets fully amortized in 2008 and therefore no expense incurred in the period, and an overall reduction in the asset base used in the calculation of amortization expense using the declining-balance method combined with no new capital expenditures in the period.

Interest income

Interest income for the three months ended December 31, 2009 was \$3,210, representing a decrease of \$2,593 or 209%, from \$5,803 for the same period in 2008. This decrease was primarily due to lower average cash balance in the period as compared to the same period in 2008.

Foreign Exchange Translation

Loss due to foreign exchange translation on balance sheet on items such as Accounts Receivable, Accounts Payable and foreign bank accounts was \$180,820 for the three months ended December 31, 2009, an increase of \$401,066 from a translation gain of \$220,246 for the same period in 2008.

Net loss

Net loss for the three months ended December 31, 2009 was \$752,277 or \$nil per share, representing an improvement of \$77,258, or 9%, from a net loss of \$829,535 or \$nil per share for the same period in 2008.

Net loss before interest income, foreign exchange translation and proxy contest charges for the three months ended December 31, 2009 was \$574,667 representing an improvement of \$424,917 or 43% from \$999,584 for the same period in 2008.

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 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 thousand of Canadian dollars, except per share data)

	Dec 31 2009	Sept 30 2009	June 30 2009	Mar 31 2009	Dec 31 2008	Sept 30 2008	June 30 2008	Mar 31 2008
STATEMENT OF OPERATIONS								
Revenues								
Devices	\$ 751	\$ 703	\$ 1,017	\$ 101	\$ 25	\$ 287	\$ 55	\$ 78
Services	944	790	566	338	307	171	130	116
Total revenues	1,695	1,493	1,583	439	332	458	185	194
Cost of revenues	288	482	903	120	164	286	180	171
Gross margin (loss)	1,407	1,011	680	319	168	172	5	23
Operating expenses								
General administration	989	506	438	484	483	656	677	701
Research and development	457	444	456	475	410	398	519	509
Selling and marketing	479	404	329	281	277	339	380	317
Stock-based compensation	27	70	62	51	18	56	66	152
Amortization	29	31	29	32	36	50	62	66
Total operating expenses	1,981	1,455	1,314	1,323	1,224	1,499	1,704	1,745
Loss before under noted	(574)	(444)	(634)	(1,004)	(1,056)	(1,327)	(1,699)	(1,722)
Interest income	3	3	3	3	6	10	23	42
Foreign exchange translation	(181)	(137)	12	57	220	13	(4)	47
Proxy contest	-	(515)	-	-	-	-	-	-
Write-off of investment	-	-	-	-	-	-	-	-
Net loss for the period	\$ (752)	\$ (1,093)	\$ (619)	\$ (944)	\$ (830)	\$ (1,304)	\$ (1,680)	\$ (1,633)
Loss per share	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)
CASH FLOW INFORMATION								
Operating activities	\$ (557)	\$ (935)	\$ 492	\$ (1,359)	\$ 548	\$ (1,328)	\$ (1,784)	\$ (1,526)
Investing activities	895	(5)	(3)	(3)	(4)	(3)	(47)	(46)
Financing activities	(2)	-	-	(3)	(9)	99	(30)	(54)
Net cash inflow (outflow)	336	(940)	489	(1,365)	535	(1,232)	(1,861)	(1,626)
Cash, beginning of period	304	1,244	755	2,120	1,585	2,817	4,677	6,303
Cash, end of period	\$ 640	\$ 304	\$ 1,244	\$ 755	\$ 2,120	\$ 1,585	\$ 2,816	\$ 4,677
BALANCE SHEET INFORMATION								
Working capital (deficiency)	\$ (1,622)	\$ (624)	\$ 558	\$ 608	\$ 1,433	\$ 2,162	\$ 3,262	\$ 4,807
Total assets	\$ 2,041	\$ 3,526	\$ 2,784	\$ 2,865	\$ 4,221	\$ 4,382	\$ 5,028	\$ 6,778
Shareholders' equity (deficiency)	\$ (1,580)	\$ (877)	\$ 163	\$ 698	\$ 1,591	\$ 2,403	\$ 3,552	\$ 5,167

The Company's revenues and financial results are difficult to forecast and have historically fluctuated on a quarterly basis, and it is expected that quarterly revenues and financial results will continue to fluctuate in the future as the Company continues growing into the marketing and commercialization stage. Fluctuations in results related to the growth of the Company's revenues, the timing of revenues being recognized and sales to customers, which may place large

single orders in any one quarter, and to the timing of staffing and infrastructure additions to support growth.

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 revenues; 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 for the year ended December 31, 2009 was \$3,050,762 (which includes non-recurring proxy contest charges of \$514,694), compared to \$4,825,769 in the same period in 2008, representing an improvement of \$1,775,007. Cash used in the day to day operations for the year ended December 31, 2009 was \$2,368,903 (which includes non-recurring charges of \$514,694) compared to \$4,089,460 in the same period in 2008, representing a decrease and improvement of \$1,720,567, which was combined with a decrease in cash provided by non-cash working capital activities of \$54,450 such as: an increase in cash provided by inventory of \$1,158,283, accounts payable and accrued liabilities of \$550,048, and prepaid expenses of \$153,679, offset by cash used by accounts receivable of \$442,888 and other receivables of \$16,607, and by deferred revenues of \$1,456,965.

Cash flow used in investing activities

Cash flow used in investing activities for the year ended December 31, 2009 was \$891,315 compared to \$99,673 in the same period in 2008, representing an increase in the inflow of cash of \$990,988. The increase can be attributed to a short term loan the Company put in place with a financial institution.

Cash flow provided by financing activities

Cash outflow by financing activities for the year ended December 31, 2009 was \$2,700 compared to cash flow of \$6,115 for the same period in 2008, representing a decrease in cash provided of \$8,815.

The cash balance of the Company at December 31, 2009 was \$640,055, a decrease of \$1,480,278 from December 31, 2008. Current assets at December 31, 2009 were \$1,965,987 compared to \$4,014,942 at December 31, 2008. Working capital decreased by \$3,054,825 to a deficiency of \$1,621,815 as of December 31, 2009 from \$1,433,010 in working capital as of December 31, 2008.

The Company's current business plan and sales forecast projects revenue growth in 2010. The Company believes that its advancement of its DEFIMENTTM transaction with the United States Department of Homeland Security will lead to future opportunities within other departments in the United States Government, and also abroad with other governments as well as continued growth with the United States Department of Homeland Security.

The Company's need for capital expenditures is limited to such items as computer hardware and software, expenditures to support sales, marketing and general administration activities and working capital. Since inception, the Company has financed its cash and/or capital requirements through the issuance of equity from private placements and through the issuance of obligations under capital leases. Until the Company starts generating and receiving significant revenues and the resulting cash flow from the sales of its devices and services the primary source of funding for the Company will continue to be external sources of capital including the issuance of debt and equity, which given the current economic times could prove to be difficult.

On an ongoing basis, the Company investigates various financing options, including a credit facility and/or additional equity financings as well as other strategic funding sources to fund the continuing efforts to commercialize its devices and services. These events may or may not happen depending on the availability of funds under acceptable terms and conditions, the availability of equity capital and the price at which additional equity could be issued. Recurring capital is dependent upon the success of the Company and upon the state of the capital markets in general.

The Company has a \$2,500,000 (Dec. 31, 2008 - \$nil) non-revolving senior credit facility that bears interest at bank prime plus 2.5% per annum. As of December 31, 2009, the Company had utilized \$854,717 (2008 - \$nil) of this credit facility. The credit facility's term was to have expired and the amount fully repaid on February 28, 2010.

On February 23, 2010, the Company was granted an extension on the repayment of its obligation from February 28, 2010 to May 31, 2010. At the same time the non-revolving senior credit facility was reduced from \$2,500,000 to \$1,000,000. Based on the extension being granted, at the request of the lender, the Company agreed to pay an extension fee of \$10,000 and initiate monthly principal payments of \$10,000 per month commencing February 28, 2010 until the outstanding balance is fully repaid on May 31, 2010.

As at December 31, 2009, the Company was in violation of a financial covenant, specifically its minimum current ratio (current assets divided by current liabilities). The lender has provided the Company with a waiver for the covenant breach that is in force until May 31, 2010. Interest expense related to this credit facility for the year ended December 31, 2009 was \$8,003 (2008-\$nil).

The following table discloses future payments as at December 31, 2009 committed by the Company over the next five (5) years. It includes both principal and interest obligation 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
Operating leases	\$ 132,000	\$ 120,000	\$ 12,000	\$ -	\$ -

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 December 31, 2009, 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.

TRANSACTIONS WITH RELATED PARTIES

The Company had the following transactions and/or outstanding amounts with related parties for the year ended December 31, 2009:

- Recorded interest income of \$5,100 for the year ended December 31, 2009, 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, The debtor has committed to repaying the loan no later than April 19, 2010 . As at December 31, 2009, the total outstanding amount including interest amounted to \$95,200.
- Recorded interest income of \$2,860 for the year ended December 31, 2009, related to \$52,000 advance in terms of a promissory note dated December 27, 2007 to a former officer, the Executive Vice President and COO, of the Company, secured and due on demand bearing interest at 6% per annum. The loan was repaid in full on December 18, 2009.
- Recorded interest income of \$3,000 for the year ended December 31, 2009, 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. The Executive Vice President and CTO has committed to repaying the loan no later than April 19, 2010. As at December 31, 2009 the total outstanding amount including interest amounted to \$50,000.
- Recorded interest income of \$626 for the year ended December 31, 2009, 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. The Executive Vice President and CTO has committed to repaying the loan no later than April 19, 2010. As at December 31, 2009 the total outstanding amount including interest amounted to \$27,800.
- Recorded proxy contest charges related to the Annual and Special Shareholders Meeting held on September 24, 2009 for a payment made to the former President and CEO of the Company for reimbursement of costs incurred for third party service providers, including but not limited to consulting, printing, mailing, and transfer agent services, in the amount of \$514,694 in the year ended December 31, 2009. These charges are one-time charges in nature not expected to recur.
- The Company made payments to 1220764 Ontario Inc. for management services provided by Mr. Tony P. Busseri, a director of the Company \$33,750 in the year ended December 31, 2009.

PROPOSED TRANSACTIONS

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

CRITICAL ACCOUNTING ESTIMATES

The Company's consolidated financial statements as at and for the year ended December 31, 2009 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. MobiKEY®) sales and subscription services (i.e. TruOFFICE™). The Company recognizes revenue in accordance with EIC 141, "Revenue Recognition", and EIC 142, "Revenue Arrangements with Multiple Deliverables".
- 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

Goodwill and Intangible Assets

In February 2008, the CICA issued Handbook Section 3064, *Goodwill and Intangible Assets* which supersedes Sections 3062 *Goodwill and Other Intangible Assets*. Section 3064 provides additional guidance on when expenditures qualify for recognition as intangible assets and requires that costs be deferred only when relating to an item meeting the asset definition. CICA Handbook Section 1000, Financial Statement Concepts, was also amended to provide consistency with this new standard. The Company adopted this standard for the fiscal year commencing January 1, 2009. The adoption of this standard has had no material impact on the Company's financial statements or disclosures.

Financial Instruments

The Company also adopted the changes made by CICA to Section 3862, *Financial instruments – Disclosures* whereby an entity shall classify and disclose fair value measurements using a fair

value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy shall have the following levels:

Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

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); and

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.

In January 2009, the Company adopted Emerging Issues Committee (“EIC”) 173, Credit risk and the fair value of financial assets and financial liabilities issued by the Emerging Issues Committee. This abstract requires that an entity's own credit risk (for financial liabilities) and the credit risk of the counterparty (for financial assets) should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. The adoption of this abstract did not have a material impact on the consolidated financial statements.

FUTURE ACCOUNTING PRONOUNCEMENTS

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, this 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 will

include 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 ensuring that comparative results for fiscal year 2010 will be available when preparing the 2011 financial reports. Changes implemented when converting to IFRS will be reported in 2010's 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 will be 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 preliminary planning and scoping and diagnostic phase and Impact analysis, evaluation and design phase in 2009. The Company has drafted technical papers and is in the process of selecting accounting policies. The Company has identified the areas noted below as those expected to have the most significant impact on its financial statements. 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.

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 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.

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 impact to recorded amounts is expected upon conversion to IFRS.

Impairment of Non-Financial Assets

Under IFRS, an entity must assess at each reporting date whether there is any indication that an asset might be impaired. If any such indication exists, the entity must estimate the recoverable amount of the asset, which is defined as the higher of an asset's or cash generating unit's ("CGU") fair value less costs to sell and its value in use. Value in use is the present value of the future cash flows expected to be derived from an asset or CGU. An impairment loss must be recorded if the carrying value of the asset or CGU is more than the recoverable amount of the asset or CGU. The first step in recognition of an impairment loss under Canadian GAAP is based on undiscounted cash flows, which does not exist under IFRS. Therefore an impairment loss could be recognized under IFRS earlier than under Canadian GAAP.

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 December 31, 2009 and December 31, 2008:

	December 31, 2009		December 31, 2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
FINANCIAL ASSET				
Held for trading				
Cash (i)	\$ 640,045	\$ 640,045	\$ 2,120,333	\$ 2,120,333
Loans and receivables				
Accounts receivable (i)	\$ 88,583	\$ 88,583	\$ 115,620	\$ 115,620
Other receivables (i)	\$ 34,954	\$ 34,954	\$ 18,873	\$ 18,873
Notes receivable (i)	\$ 173,000	\$ 173,000	\$ 198,220	\$ 198,220
FINANCIAL LIABILITIES				
Other liabilities				
Accounts payable and accrued liabilities (i)	\$ 1,197,258	\$ 1,197,258	\$ 920,541	\$ 920,541
Bank Indebtedness	\$ 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
Financial assets				
Cash	\$ 640,045	\$ -	-	\$ 640,045
Total financial assets	\$ 640,045	\$ -	-	\$ 640,045
Financial liabilities				
Total financial liabilities	-	-	-	-

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.

	Risks			
	Credit	Liquidity	Foreign Exchange	Interest Rate
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 year ended December 31, 2009, the largest single customer represented approximately 37% of recorded revenues.

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 December 31, 2009, the Company had cash consisting of cash on hand and deposits with banks of \$640,045 (December 31, 2008 - \$2,120,333). During the year ended December 30, 2009, 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 December 31, 2009, the largest single customer represented approximately 6.2% of accounts receivable.

The following table outlines the details of the aging of the Company's receivables as at December 31, 2009 and December 31, 2008:

	December 31, 2009	December 31, 2008
Current	\$ 31,427	\$19,882
Past due		
1 – 60 days	47,873	15,244
Greater than 60 days	27,743	180,554
Less: Allowance for doubtful accounts	(18,460)	(100,060)
Total accounts receivable, net	\$ 88,583	\$115,620

The following table outlines the details of the Allowance for Doubtful Accounts of the Company's receivables as at December 31, 2009 and December 31, 2008:

	December 31, 2009	December 31, 2008
Opening balance as of January 1, 2009	\$ (99,672)	\$ (122,612)
Collected in period	1,297	-
Increase in reserve in period	(2,769)	(52,064)
Write-off in period	82,684	75,004
Closing balance as of December 31, 2009	\$ (18,460)	\$ (99,672)

(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 December 31, 2009:

	2010	2011	Total
Accounts payable and accrued	\$ 1,197,258	\$ -	\$ 1,197,258
Bank Indebtedness	854,717	-	854,717
Operating lease commitments	120,000	12,000	\$ 132,000
	\$ 2,171,975	\$ 12,000	\$ 2,183,975

(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 December 31, 2009, the Company's had non-Canadian dollar net monetary liabilities of approximately US\$271,400 and €136,700 (December 31, 2008 - approximately US\$26,300 and €34,000), any changes in the respective exchange rates as at December 31, 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 December 31, 2009, cash totalled \$640,045 (December 31, 2008 - \$2,120,333). An increase of 100 basis points in the market interest rate would have decreased net loss by approximately \$6,400 (a 100 basis point decrease would have had the equal but opposite effect) for the year ended December 31, 2009.

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
- 70,360,333 common share purchase warrants ("Warrants") convertible into 32,360,333 common shares
 - 36,243,573 Warrants at \$0.155/share expiring November 7, 2009. On October 8, 2009, the TSX Venture Exchange has approved an extension to the expiry date of 32,360,333 Warrants, from November 7, 2009 to May 7, 2010.
 - 38,000,000 Warrants at \$0.15/share expiring on February 26, 2015
- 30,025,000 common share purchase options ("**Options**") convertible into 30,025,000 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

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 in the marketplace on reasonable terms for a company of our size and financial status for short term working capital purposes. Access to such financing at acceptable commercial terms for a company of our size and financial status will be dependent on the timing of recognition and receipt of cash from our current backlog, on our ability to demonstrate execution of our business strategy and the general condition of the credit and/or equity markets and may be significantly dilutive to existing shareholders.
- The Company's access to credit or capital could be further restricted by the 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 largely expected to arise from the US\$1.4 million renewal of the DEFIMNET™ service with the Reseller. If the Reseller were to discontinue its relationship with the Company, or if the Company were to otherwise be involved in any disagreement or dispute with the Reseller over the Company's service performance, the Company would look at alternative reseller relationships to continue servicing the U.S. Department of Homeland Security and such event may have a material adverse impact on the Company's financial results.
- There is no assurance that any forward-looking statement will materialize.
- The results or events predicted herein may differ from the actual results or events.
- 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 a working capital deficiency at December 31, 2009 of \$1,621,815, 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, could 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, could also harm the Company's competitive advantage in the secure remote access industry;
- Route1's ability to obtain rights to use software or components supplied by third parties, which may not be sufficient to support future sales volumes;
- Route1's ability to enhance current products and develop and introduce new products; that could hinder the Company's continued growth;
- The efficient and uninterrupted operation of Route1's MobiNET®, 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 hamper the Company's continued growth;

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- The occurrence or perception of a breach of Route1's secure product and service offering, or an inappropriate disclosure of confidential information, which could also impact on the credibility of the Company's product and services;
 - Intense competition within the secure remote access industry that could hamper future sales volumes;
 - Route1's reliance on its suppliers and the risk that suppliers will not be able to deliver components on a timely basis, which may not be sufficient to support future sales volumes;
 - Effective management of growth and on-going development of the business;
 - The market price of the Route1's common shares could be subject to wide fluctuations in response to Route1's financial results, changes in earnings estimates by analysts, changing conditions in the identity access management sector or changes in general market, economic or political conditions;
 - Route1's articles permit the issuance of an unlimited number of common shares and if the Company was to issue a significant number of common shares, it would reduce the relative voting power of previously outstanding common shares. Such future issuances could be at prices less than some or all shareholders paid for their common shares of the Company. Significant issuance of Route1's common shares, or the perception that such issuances may occur, could impact, negatively or otherwise, the trading price of Route1's common shares;
 - As of the date hereof, Route1's directors and executive officers and entities affiliated with them owned approximately 15% of the outstanding share of common shares, not including options or warrants to purchase shares of common shares. As a result, these shareholders, acting together, may be able to influence or control matters requiring approval by our shareholders, including the election of directors, the adoption of equity incentive plans and the approval of mergers or other extraordinary transactions. These shareholders may have interests that differ from shareholders with smaller holdings. The concentration of ownership of Route1's common shares could have the effect of delaying, preventing or deferring a change in control of Route1, deprive its shareholder of an opportunity to receive a premium for their common shares as part of a sale of Route1 and affect the market price of its common shares; and
 - Government regulation of secure remote access industry, including but not limited to restrictions on encryption of MobiKEY® and the MobiNET®.
 - Economic downturn that may cause 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 meet the qualifications of a financial expert.

Legal proceedings

The Company filed Statements of Claim against certain reseller customers relating to non-payment of invoices in January 2008. The reseller customers have 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®s

that were delivered in 2007 for which revenue of approximately \$333,000 was 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 proceeding is ongoing as of the date of this report with the other reseller customer.

PROXY CONTEST CHARGES

The proxy contest charges of \$514,694 include legal fees, proxy solicitation fees and expenses, and other professional consulting fees relating to the September 24, 2009 Annual and Special Shareholders Meeting, which was a contested meeting. These charges are expected to be one time in nature and not to recur.

SUBSEQUENT EVENTS

On January 11, 2010, Route1 Inc announced that the Reseller informed the Company that it would not be respecting its contractual obligations under the Agreement in regards to their purchase of the remaining Minimum Amount of approximately 25,000 MobiKEY[®] devices. 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. The Company 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 purchase the remaining Minimum Amount.

On February 26, 2010 the Company announced the closing of a non-brokered private placement of 38,000,000 units (the "Units") at \$0.05 per Unit for aggregate net proceeds of CDN\$1,900,000. Each Unit is comprised of one common share and one common share purchase warrant of the Company. 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 following the closing date.

On March 1, 2010, the Company announced that a total of 9,500,000 stock options to purchase common shares of Route1 were granted to an officer and a consultant of Route1 on February 26, 2010 and expiring on February 26, 2015. 5,250,000 of the stock options are exercisable at \$0.10 per share and 4,250,000 are exercisable at \$0.15 per share. The grant is subject to regulatory approval.

On March 25, 2010 the Company announced that a total of 12,525,000 stock options to purchase common shares of Route1 were granted to employees, officers and a director of Route1 on March 24, 2010 at an exercise price of \$0.13 per share, expiring on March 24, 2015. The grant is subject to regulatory approval.

Additional Information

Additional information about Route1 is available from Route1's website at www.route1.com, the SEDAR website at 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).