
ROUTE1 INC.

MANAGEMENT DISCUSSION AND ANALYSIS

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2011

As at November 24, 2011

The following discussion and analysis of the financial condition and results of operations (this “**MD&A**”) of Route1 Inc. (also referred to as “**we**”, “**us**”, “**our**”, “**Route1**”, or the “**Company**”), should be read in conjunction with the Company’s third quarter 2011 unaudited interim condensed consolidated financial statements. The Company’s third quarter 2011 unaudited condensed interim consolidated financial statements and the accompanying notes form part of the first annual audited consolidated financial statements to be prepared in accordance with International Financial Reporting Standards (“**IFRS**”) for the year ended December 31, 2011 and have been prepared in accordance with International Accounting Standard (“**IAS**”) 34, “Interim Financial Reporting” as issued by the International Accounting Standards Board (“**IASB**”) and using the accounting policies described therein. This Management Discussion & Analysis (“**MD&A**”) has been reviewed and approved by the Company’s Board of Directors prior to filing.

The information in this MD&A is current to November 24, 2011, unless otherwise noted.

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 obligations, 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, and that has not been otherwise disclosed in other filings, is material in nature.

INTELLECTUAL PROPERTY NOTICES

© Route1 Inc., 2011. All rights reserved. Route1, the Route1 and shield design Logo, SECURING THE DIGITAL WORLD, Mobi, MobiSecure, Route1 MobiKEY, Route1 MobiVDI, MobiKEY, MobiKEY IBAD, DEFIMNET, MobiNET, Route1 MobiNET, TruOFFICE, TruFLASH, TruOFFICE VDI, MobiKEY Fusion, EnterpriseLIVE, EnterpriseLIVE VO, MobiNET Agent and MobiKEY Classic, are either registered trademarks or trademarks of Route1 Inc. in the United States and or Canada. All other trademarks and trade names are the property of their respective owners. The DEFIMNET and MobiNET platforms and the MobiKEY, MobiKEY Classic and MobiKEY Fusion devices are protected by U.S. Patents 7,814,216 and 7,739,726, and other patents pending.

OVERVIEW

Route1 delivers industry-leading security and identity management solutions to corporations and government agencies that need universal, secure access to all digital resources and sensitive data. These customers depend on The Power of MobiNET - Route1's communications and service delivery platform. MobiNET provides identity assurance and individualized access to networks and data. Route1's patented solutions simplify the process of meeting increasingly stringent regulatory requirements for privacy and security.

HIGHLIGHTS

- On April 29, 2011, the Company announced that it has been awarded a blanket purchase agreement by the United States Department of the Interior, U.S. Fish and Wildlife Service ("FWS"). FWS has entered into a blanket purchase agreement with Route1 for delivery of up to 10,000 users, with the longer-term goal of adding users from other components of the United States Department of the Interior. The term of the blanket purchase agreement is five years from the date of the award, with the total value of the agreement valued at US\$25 million. This award was a result of a pilot program conducted in 2010 by FWS, with a limited number of users, to evaluate Route1's security and identity management solution. The Company signed the agreement on May 2, 2011.
- On May 31, 2011, the Company announced the release of its TruOFFICE 3.0 software application with expanded and improved enterprise tools. TruOFFICE 3.0 users will now be notified directly through their MobiKEY Classic or MobiKEY Fusion device that an application software update is available. When the user accepts the update from any internet-enabled computer, the secure software application update will be performed. TruOFFICE 3.0 also now provides enterprise clients with additional tools that will simplify the provisioning and administration of users, improve the functionality of Route1 secure remote access solution, enhance security measures, and expand the solution use cases.
- On June 24, 2011, the Company announced that the outside contractor that provides the vast majority of required information technology services to the U.S. Navy (the "Contractor"), has informed it that the U.S. Navy can now procure Route1's secure remote access solution, effective immediately. Under the

terms of an agreement between the Contractor and Route1, Route1 will sell its integrated security and identity management solution (the "Route1 Solution") to the Contractor and the Contractor will resell the Route1 Solution to the U.S. Navy. The Agreement includes all traditional terms and conditions that would be found in a sub-contractor agreement including but not limited to (a) the DEFIMNET platform to be used is the platform located in Norfolk, Virginia that was used for Route1's pilot project with the U.S. Navy, (b) the maximum number of permissible TruOFFICE application software licenses issued and associated users registered with the DEFIMNET platform will be 5,000, and (c) Route1 expects to generate revenue from the sale of additional MobiKEY Fusion devices and monthly recurring service fees for the use of the DEFIMNET platform and TruOFFICE application software licenses. Assuming 5,000 subscribers over a full one year term and the procurement of an additional 4,600 MobiKEY Fusion devices, the Agreement will generate in excess of C\$2.5 million in hardware and services revenue to Route1.

- On August 25, 2011, the Company announced that the United States (U.S.) Navy has ordered 1,206 subscriptions of its comprehensive solutions, which are in the process of being provisioned. This deployment for the U.S. Navy is comprised of Route1's private communications and service delivery platform, the DEFIMNET, its TruOFFICE application software, and its MobiKEY Fusion device. The Company expects the U.S. Navy's usage of the Route1 Solution to continue to expand and expects the maximum number of permissible TruOFFICE application software licenses and associated users registered with the DEFIMNET platform of 5,000, to be procured and provisioned during the fourth quarter of the current calendar year. These 5,000 members of the U.S. Navy will be empowered to access their digital resources remotely without risk of their data being compromised.
- On September 15, 2011, the Company announced that it responded to reports of an application by Qwest Government Services, Inc. ("Qwest") in the District of Columbia District Court ("District Court") for letters rogatory. This was purely a procedural step to ask a Judge of the District Court to request the Ontario Superior Court to issue summonses to witnesses in Ontario to testify in a private, ongoing arbitration between Route1 and Qwest. Further, the step does not seek any relief against Route1. The arbitration was brought by Route1 against Qwest on December 14, 2010 under the Federal Reseller Agreement between the parties made as of May 9, 2008, and as amended on November 25, 2008 (the "Agreement"). Under the terms of the Agreement, the arbitration of disputes between the parties is confidential.
- On September 22, 2011, the Company reported the success of its TruOFFICE Virtual Desktop Infrastructure (VDI) solution, which answers the call from enterprise and government organizations for secure, remote desktop management. TruOFFICE VDI, powered by Route1's patented identity assurance and management technology, integrates directly into traditional desktop virtualization solutions to offer an unparalleled level of security. Unlike other offerings that authenticate only against a remote computer or device, Route1 utilizes multiple verifications to guarantee a specific individual's identity. The Company's one-of-a-kind solution delivers remote users the identical access to their desktops and content as if they were onsite, and enables them to work seamlessly on their virtual or physical office computers. Most important to note, is that TruOFFICE VDI prevents any file transfer to external locations; content and information remain protected and kept within the enterprise firewalls.
- On September 26, 2011, the Company announced that it received approval for all proposals submitted to stockholders at the Company's annual meeting, which was held on September 26, 2011 in Toronto, Ontario. The matters voted on and approved were (1) Tony P. Busseri, Peter F. Chodos, Amar S. Doman, Michael F. Doolan and Michael D. Harris were elected as the Company's directors, (2)

Deloitte & Touche LLP Chartered Accountants was reappointed as the Company's auditors in respect of the year ending December 31, 2011, (3) The shareholder rights plan, which was approved by the Board of Directors and announced in the Company's second quarter financial results release on August 25, 2011, has been approved, and (4) the Company's stock option plan was voted on and reapproved. Each of the four matters that were voted on received greater than 88% approval, with a total of 189.3 million shares voted at the meeting.

NON-IFRS 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 IFRS 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 effect of amortization expense because it is largely dependent on the accounting methods and assumptions we use.

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 IFRS financial measure is *operating profit (loss) for the period*, which is discussed below. The table below reconciles EBITDA to Operating profit (loss) for the period for the quarters presented.

<i>In thousands of Canadian dollars</i>	Sept 30 2011	June 30 2011	Mar 31 2011	Dec 31 2010	Sept 30 2010
EBITDA	(36)	70	205	440	(284)
Amortization	34	40	51	35	23
Operating (loss) profit	(71)	30	154	405	(307)

GOING CONCERN ASSUMPTION

Our unaudited condensed interim 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 and nine months ended September 30, 2011, the Company incurred a net loss of \$626,435 and \$829,652 respectively, and as at September 30, 2011 had an accumulated deficit of \$37,141,708 and shareholders' deficiency of \$585,720. 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.

SELECTED FINANCIAL INFORMATION

The following table outlines selected financial information of the Company on a consolidated basis for the three and nine months ended September 30, 2011 and 2010.

Results of Operations

(in thousands of Canadian dollars, except per share amounts)

	For the three months ended		For the nine months ended	
	Sept 30, 2011	Sept 30, 2010	Sept 30, 2011	Sept 30, 2010
STATEMENT OF OPERATIONS				
Revenue				
Devices and appliances	\$173	\$386	\$464	\$644
Services	1,226	995	3,591	2,949
Total Revenue	1,399	1,381	4,055	3,593
Cost of revenue	266	350	762	595
Gross profit	1,133	1,031	3,293	2,998
Operating expenses				
General administration	760	633	2,139	1,735
Research and development	261	521	570	1,413
Selling and marketing	183	184	471	542
Total operating expenses	1,204	1,338	3,180	3,690
Operating (loss) profit for the period	(71)	(307)	113	(692)
Stock-based compensation	(362)	(380)	(767)	(824)
Interest income	-	-	1	4
Interest (expense)	(4)	-	(5)	(20)
Foreign exchange translation	71	(12)	89	(113)
Severance charges	(261)	(460)	(261)	(460)
Total comprehensive (loss) gain for the period	\$(627)	\$(1,159)	\$(830)	\$(2,105)
Loss per share	\$(0.00)	\$(0.00)	\$(0.00)	\$(0.00)
CASH FLOW INFORMATION				
Operating activities	\$(229)	\$(733)	\$(367)	\$(1,517)
Investing activities	(106)	(57)	(188)	(3)
Financing activities	104	-	69	1,027
Net cash inflow (outflow)	(231)	(790)	(486)	(493)
Cash, beginning of period	255	937	484	640
Cash, end of period	\$24	\$147	\$(2)	\$147
Working capital (deficiency)	\$(853)	\$(887)	\$(853)	\$(887)
Total assets	\$2,616	\$2,437	\$2,591	\$2,437
Shareholders' deficiency	\$(586)	\$(979)	\$(586)	\$(979)

COMPARISON FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2011 AND 2010

Revenue

Revenue for the three months ended September 30, 2011 was \$1,399,163, representing an increase of \$18,416 or 1.3%, from \$1,380,747 for the same period in 2010. The comparison, discussed by segment, is as follows:

Devices and Appliances

Revenue from our devices (the MobiKEY Classic device and the MobiKEY Fusion device) and appliances (the DEFIMNET platform and the EnterpriseLIVE AG appliance) segment for the three months ended September 30, 2011 was \$173,062, representing a decrease of \$212,603 or 55.1%, from \$385,665 for the same period in the 2010. Last year, during the third quarter, there were large purchases of devices by an existing U.S. government client and the U.S. Navy. Devices and appliances revenue as a percentage of total revenue represents 12% of total revenue for the current period as compared to 28% for the prior year period.

Services

Revenue from our services segment (TruOFFICE application software, and the DEFIMNET platform and other appliance licensing or yearly maintenance) for the three months ended September 30, 2011, was \$1,226,101, representing an increase of \$231,019 or 23.2%, from \$995,082 for the same period in 2010. Services revenue, as a percentage of total revenue, represented 88% for the current period as compared to 72% for the prior year period. The increase in services revenue represents the continued growth in our TruOFFICE application software subscriber base from the same period in 2010.

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

TruOFFICE Subscribers <i>(in thousands of Canadian dollars for Revenue)</i>	Sept 30 2011	June 30 2011	Mar 31 2011	Dec 31 2010	Sept 30 2010
Closing Number	15,796	15,722	15,642	15,654	15,648
Average Number ⁽¹⁾	15,776	15,694	15,672	15,635	14,585 ⁽²⁾
Revenue per Subscriber	\$246	\$245	\$251	\$253	\$248
Revenue	\$969	\$960	\$982	\$958	\$904

⁽¹⁾ Calculated by taking the average of the closing TruOFFICE subscriber number at the end of the month for each of the three months during the quarter.

⁽²⁾ For the three months ended September 30, 2010, the ending subscriber number includes the 1,533 subscriptions sold to US DHS, CBP on September 16, 2010. Revenue recognition for the new subscriber service, as per Company policy, commenced in the month of October 2010.

The active TruOFFICE subscriber number stands at 15,796 as at November 17, 2011 plus an additional 1,335 U.S. Navy subscribers who have not yet been provisioned. The total U.S. Navy subscriber base is 1,735.

Gross Profit

Gross profit is equivalent to revenue minus the cost of revenue. The cost of revenue primarily includes the cost of our devices and appliances sold to clients, as well as the cost of their shipping and packaging, plus the cost to operate and maintain the Route1 MobiNET platform.

The cost of revenue for the three months ended September 30, 2011 was \$266,137, representing a decrease of \$83,330 from \$349,467 for the same period in 2010. The decrease in cost of revenue for the three months ended September 30, 2011 is a result of lower device sales during the third quarter of 2011 as compared to the same period in 2010, resulting in lower operational costs.

Gross profit for the three months ended September 30, 2011 was \$1,133,026 or 81% of gross revenue, representing an increase of \$101,746 from a gross margin of \$1,031,280 or 75% of gross revenue for the same period in 2010. The increase in gross profit is attributable to higher margins realized on Service segment revenue offset partially by a higher accrual amount for royalties on licenses.

The gross margin percentage for each of the prior five quarters is provided below:

	Q3 2011	Q2 2011	Q1 2011	Q4 2010	Q3 2010
Gross profit percentage	81%	77%	85%	96%	75%

Expenses

Operating expenses consist of general administration, research and development, and selling and marketing. Operating expenses for the three months ended September 30, 2011 were \$1,203,844, representing a decrease of \$134,364 or approximately 10%, from \$1,338,208 for the same period in 2010.

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, depreciation and amortization and other indirect costs.

General administration expenses for the three months ended September 30, 2011 were \$759,734, representing an increase of \$127,087 or approximately 20%, from \$632,647 for the same period in 2010 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses increased by approximately \$121,000 for the three months ended September 30, 2011 as compared to the same period in 2010, primarily as a result of reclassifying certain employees and management from other departments as well as increases to compensation for certain employees effective January 2011; and
- Audit expenses decreased by approximately \$14,000 for the three months ended September 30, 2011 as compared to the same period in 2010, primarily as a result of timing differences in expenses incurred for the preparation of the Scientific Research and Development filing in 2010 compared to this year; and
- Legal expenses increased by approximately \$35,000 for the three months ended September 30, 2011 as compared to the same period in 2010, primarily as a result of expenses incurred for preparation of the shareholder rights plan and expenses incurred for the settlement of severance for a previous officer of the Company.

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, 2011 were \$261,526, representing a decrease of \$260,041 or approximately 50%, from \$521,567 for the same period in 2010 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses decreased by approximately \$249,000 for the three months ended September 30, 2011 as compared to the same period in 2010, as a result of a decrease in head count in this department as well as reclassifying of certain employees and management.
- There was an additional expense for filing the Scientific Research and Development return in the 2010 year of \$11,200.

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, 2011 were \$182,584, relatively flat from \$183,994 for the same period in 2010.

Other Items

Stock-based compensation

Stock-based compensation was \$361,865 for the three months ended September 30, 2011, a decrease of \$17,979 from \$379,844 for the same period in 2010. The contributing factors to the decrease were the reduction in expenses due to a percentage of options vesting during the third quarter of 2011.

Interest income

Interest income for the three months ended September 30, 2011 was \$450, representing an increase of \$429 from interest income of \$21 for the same period in 2010. Interest income represents interest generated from cash and cash equivalent balances the Company maintains with financial institutions.

Interest expense

Interest expense for the three months ended September 30, 2011 was \$4,722, representing an increase of \$4,248 from interest expense of \$474 for the same period in 2010. The increase in interest expense from prior year is due to the interest paid to a financial institution with respect to the use of the credit facility during the third quarter of 2011.

Foreign exchange translation

The gain attributable to foreign exchange translation on balance sheet items such as Accounts Receivable, Accounts Payable and foreign bank accounts was \$71,473 for the for the three months ended September 30, 2011, an increase of \$83,026 from a loss of \$11,553 for the same period in 2010. There was significant volatility and fluctuation of the Canadian dollar against the Euro and U.S. dollar during the third quarter of the current year.

Severance charges

Severance charges for the three months ended September 30, 2011 were \$260,953 and were a one-time expense the Company incurred to terminate the employment agreement of the Company's former Chief Technology Officer. Payment of this liability is being made on a monthly payment schedule and the liability will be fully discharged by January 31, 2013. Severance charges for the three months ended September 30, 2010 were \$460,000 and were a one-time expense the Company incurred to terminate the employment agreement of the Company's former President and CEO. Payment of this liability is being made on a bi-monthly payment schedule and the liability will be fully discharged by August 31, 2012.

Comprehensive gain (loss)

Comprehensive loss for the three months ended September 30, 2011 was \$626,435 or \$0.00 per share, representing an improvement of \$532,343 from a comprehensive loss of \$1,158,778 or \$0.00 per share for the same period in 2010.

COMPARISON FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2011 AND 2010

Revenue

Revenue for the nine months ended September 30, 2011 was \$4,054,757, representing an increase of \$461,560 or 12.8%, from \$3,593,197 for the same period in 2010. The comparison, discussed by segment, is as follows:

Devices and Appliances

Revenue from our devices (the MobiKEY Classic device and the MobiKEY Fusion device) and appliances (the DEFIMNET platform and the EnterpriseLIVE AG appliance) segment for the nine months ended September 30, 2011 was \$463,734, representing a decrease of \$180,377 or 28%, from \$644,111 for the same period in the 2010. Devices and appliances revenue as a percentage of total revenue represents 11% of total revenue for the current period as compared to 18% for the prior period. The primary contributing factor to the decrease in devices and appliances revenue for the nine months ended September 30, 2011, was the higher number of devices sold to a U.S. government client and the US Navy last year.

Services

Revenue from our services segment (TruOFFICE application software, and the DEFIMNET platform and other appliance licensing or yearly maintenance) for the nine months ended September 30, 2011, was \$3,591,023, representing an increase of \$641,937 or 22%, from \$2,949,086 for the same period in 2010. Services revenue, as a percentage of total revenue, represented 89% for the current period as compared to 82% for the prior period. The increase in services revenue represents the continued growth in our TruOFFICE application software subscriber base from the same period in 2010.

Deferred revenue as at September 30, 2011 increased by \$346,092 to \$2,068,233 from \$1,722,141 as at December 31, 2010. The increase in the carrying amount of deferred revenue is primarily driven by the timing of the expiration date of certain large clients TruOFFICE subscriptions, the term length of the renewal compared with the prior term length, and to a lesser extent, as a result of the strengthening of the Canadian dollar against the U.S. dollar where 68.1% of the Company's revenue is generated. The deferred revenue is recognized into income in the period that such services are delivered and/or performed.

Gross Profit

Gross profit is equivalent to revenue minus the cost of revenue. The cost of revenue primarily includes the cost of our devices and appliances sold to clients, as well as the cost of their shipping and packaging, plus the cost to operate and maintain the Route1 MobiNET platform.

The cost of revenue for the nine months ended September 30, 2011 was \$762,174, representing an increase of \$167,450 from \$594,724 for the same period in 2010. The increase in cost of revenue for the nine months ended September 30, 2011 is a result of the higher accrual amount for royalties on licenses, increased costs for operational salaries and network costs compared to same period in 2010.

Gross profit for the nine months ended September 30, 2011 was \$3,292,583 or 81% of gross revenue, representing an increase of \$294,110 from a gross margin of \$2,998,473 or 83% of gross revenue for the same period in 2010. The increase in gross profit is attributable to a higher percentage of revenue derived from Route1's Services segment during the nine months ended September 30, 2011 compared to 2010, which generates higher profit margin than the Devices and Appliances segment. The decrease in gross profit as a percentage of gross revenue for the nine months ended September 30, 2011 is attributable to a large number of devices being sold at or near cost during the period.

Expenses

Operating expenses consist of general administration, research and development, and selling and marketing. Operating expenses for the nine months ended September 30, 2011 were \$3,179,721, representing a decrease of \$510,155 or approximately 14%, from \$3,689,876 for the same period in 2010.

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, depreciation and amortization and other indirect costs.

General administration expenses for the nine months ended September 30, 2011 were \$2,139,256, representing an increase of \$403,978 or approximately 23%, from \$1,735,278 for the same period in 2010 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses increased by approximately \$402,000 for the nine months ended September 30, 2011 as compared to the same period in 2010, primarily as a result of reclassifying certain employees and management from other departments as well as increases to compensation for certain employees effective January 2011; and
- Legal expenses increased by approximately \$84,000 for the nine months ended September 30, 2011 as compared to the same period in 2010, primarily as a result of continued work on patent applications, the familiarization of U.S. Government contract requirements, negotiation of new or expanded contracts with channel partners, and general business development requirements.
- Decreases in expenses from prior year of approximately \$82,000 can be attributed to the savings from rental equipment, telephone charges, office supplies and bank service charges.

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, 2011 were \$569,609, representing a decrease of \$843,329 or 60%, from \$1,412,938 for the same period in 2010 and the majority of the change can be summarized as follows:

- Salaries and benefits expenses decreased by approximately \$832,000 for the nine months ended September 30, 2011 as compared to the same period in 2010, as a result of a decrease in head count in this department as well as reclassifying of certain employees and management.
- The net Scientific Research and Development credit received from Revenue Canada was approximately \$11,000 higher for the nine months ended September 30, 2011 as compared to the same period in 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 nine months ended September 30, 2011 were \$470,856, representing a decrease of \$70,804 or 13%, from \$541,660 for the same period in 2010 and the majority of the change can be summarized as follows:

- Salaries, benefits and commissions expenses decreased by approximately \$187,000 for the certain employees and management as compared to the same period in 2010, primarily as a result of a reduction in head count and a lower commission payout; and
- Marketing costs, including travel expenses, brand building and tradeshow fees, increased by approximately \$116,000 as compared to the same period in 2010.

Other Items

Stock-based compensation

Stock-based compensation was \$767,108 for the nine months ended September 30, 2011, a decrease of \$57,029 from \$824,137 for the same period in 2010. The contributing factor to the decrease was the recovery of previously booked expenses for the forfeiture of unvested stock options that occurred during the nine months ended September 30, 2011 as well as a decrease in expenses due to portion of options vesting in the third quarter of 2011.

Interest income

Interest income for the nine months ended September 30, 2011 was \$1,454, representing a decrease of \$2,135 from interest income of \$3,589 for the same period in 2010. Interest income represents interest generated from cash and cash equivalent balances the Company maintains with financial institutions. The cash and cash equivalent balance for the nine months ended September 30, 2011 was lower than for the same period in 2010.

Interest expense

Interest expense for the nine months ended September 30, 2011 was \$5,227, representing a decrease of \$14,321 from interest expense of \$19,548 for the same period in 2010. The decrease in interest expense

from prior year is due to the interest paid to a financial institution with respect to the credit facility that was in place during the same period last year.

Foreign exchange translation

The gain attributable to foreign exchange translation on balance sheet items such as Accounts Receivable, Accounts Payable and foreign bank accounts was \$89,320 for the for the nine months ended September 30, 2011, an increase of \$202,666 from a loss of \$113,346 for the same period in 2010. There was significant volatility and fluctuation of the Canadian dollar against the Euro and U.S. dollar during the nine month period ended September 30, 2011.

Severance charges

Severance charges for the nine months ended September 30, 2011 were \$260,953 and were a one-time expense the Company incurred to terminate the employment agreement of the Company's former Chief Technology Officer. Payment of this liability is being made on a monthly payment schedule and the liability will be fully discharged by January 31, 2013. Severance charges for the nine months ended September 30, 2010 were \$460,000 and were a one-time expense the Company incurred to terminate the employment agreement of the Company's former President and CEO. Payment of this liability is being made on a bi-monthly payment schedule and the liability will be fully discharged by August 31, 2012.

Comprehensive loss

Comprehensive loss for the nine months ended September 30, 2011 was \$829,652 or \$0.00 per share, representing an improvement of \$1,275,193 from a comprehensive loss of \$2,104,845 or \$0.00 per share for the same period in 2010.

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 condensed interim 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 2011	June 30 2011	Mar 31 2011	Dec 31 2010	Sept 30 2010	June 30 2010	Mar 31 2010	Dec 31 2009
STATEMENT OF OPERATIONS								
Revenue								
Devices and appliances	\$ 173	\$ 171	\$ 119	\$ 22	\$ 386	\$ 212	\$ 46	\$ 751
Services	1,226	1,067	1,298	1,755	995	995	959	944
Total revenue	1,399	1,238	1,417	1,777	1,381	1,207	1,005	1,695
Cost of revenue	266	285	210	78	350	138	107	305
Gross margin (loss)	1,133	953	1,207	1,699	1,031	1,069	898	1,390
Operating expenses								
General administration	760	749	631	604	633	670	432	1,090
Research and development	261	18	290	417	521	461	430	462
Selling and marketing	183	156	132	273	184	166	192	481
Total operating expenses	1,204	923	1,053	1,294	1,338	1,297	1,054	2,033
Operating profit (loss)	(71)	30	154	405	(307)	(228)	(156)	(643)
Stock-based compensation	(362)	(300)	(105)	(377)	(380)	(331)	(113)	(20)
Interest income	-	-	1	-	-	1	2	3
Interest expense	(4)	-	-	-	-	(9)	(11)	(8)
Foreign exchange translation	71	6	11	(18)	(12)	(51)	(50)	(84)
Severance charges	(261)	-	-	-	(460)	-	-	-
Comprehensive (loss) gain for the period	\$ (627)	\$ (264)	\$ 61	\$ 10	\$ (1,159)	\$ (618)	\$ (328)	\$ (752)
Income (loss) per share	\$ (0.00)	\$ (0.00)	\$ 0.00	\$ 0.00	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)
CASH FLOW INFORMATION								
Operating activities	\$ (229)	\$ (178)	\$ (21)	\$ 418	\$ (733)	\$ 373	\$ (1,155)	\$ (557)
Investing activities	(106)	(4)	(78)	(80)	(57)	63	(10)	41
Financing activities	104	51	-	-	-	(835)	1,861	852
Net cash inflow (outflow)	(231)	(131)	(99)	338	(790)	(399)	696	336
Cash, beginning of period	255	386	485	147	937	1,336	640	304
Cash, end of period	\$ 24	\$ 255	\$ 386	\$ 485	\$ 147	\$ 937	\$ 1,336	\$ 640
BALANCE SHEET INFORMATION								
Working capital (deficiency)	\$ (853)	\$ (503)	\$ (532)	\$ (640)	\$ (887)	\$ (392)	\$ 92	\$ (1,622)
Total assets	\$ 2,616	\$ 2,011	\$ 2,134	\$ 2,272	\$ 2,437	\$ 2,753	\$ 3,481	\$ 2,041
Shareholders' equity (deficiency)	\$ (586)	\$ (340)	\$ (426)	\$ (557)	\$ (946)	\$ (92)	\$ 136	\$ (1,580)

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.

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 for the three months ended September 30, 2011 was \$230,109, compared to cash flow used of \$756,199 in the same period in 2010, representing an increase in inflow of \$526,090. Non-cash working capital activities generated \$647 for the three months ended September 30, 2011 compared to non-cash working capital generated of \$22,769 in the same period a year earlier.

Non-cash working capital for the three month period ended September 30, 2011 was negatively impacted by the investment in MobiKEY Fusion devices to support the U.S. Navy roll-out, net of sales, in the amount of \$257,576 as reflected in the increase of inventory.

Therefore net cash used in the day-to-day operations for the three months ended September 30, 2011 was \$229,462 compared to net cash used of \$733,430 in the same period in 2010, representing a decrease of usage of \$503,968.

Cash flow generated by operating activities for the nine months ended September 30, 2011 was \$62,542, compared to cash flow used of \$1,209,074 in the same period in 2010, representing an increase in inflow of \$1,271,616.

Non-cash working capital activities used \$490,084 for the nine months ended September 30, 2011 compared to \$308,295 in the same period a year earlier.

Non-cash working capital for the nine month period ended September 30, 2011 was negatively impacted by the investment in MobiKEY Fusion devices to support the U.S. Navy roll-out, net of sales, in the amount of \$257,576 as reflected in the increase of inventory.

Therefore net cash used in the day-to-day operations for the nine months ended September 30, 2011 was \$427,542 compared to \$1,517,369 in the same period in 2010, representing a decrease and improvement of \$1,089,827.

Cash flow used in investing activities

Cash flow used in investing activities for the three months ended September 30, 2011 was \$105,584 compared to cash flow used of \$56,516 in the same period in 2010, representing an increase in the outflow of cash of \$49,068. This was a result of increase in purchases for fixed assets.

Cash flow used in investing activities for the nine months ended September 30, 2011 was \$187,846 compared to cash flow used of \$2,760 in the same period in 2010, representing an increase in the outflow of cash of \$185,086. In the prior year there were proceeds to the Company of \$173,000 for repayment of Notes receivables by two former executives of the Company. This was partly offset by an increase in fixed assets of \$175,760.

Cash flow provided by financing activities

Cash flow provided by financing activities for the three months ended September 30, 2011 was \$103,959 compared to cash activity of \$nil for the same period in 2010, representing an increase in cash provided of \$103,959. The cash inflow for the three months ended September 30, 2011 is a direct result of proceeds received for the exercising of stock options and use of the Company's operating facility in the amount of \$85,434.

Cash flow provided by financing activities for the nine months ended September 30, 2011 was \$154,659 compared to cash inflow of \$1,026,778 for the same period in 2010, representing a decrease in cash provided of \$872,119. The cash inflow for the three months ended September 30, 2011 is a direct result of proceeds received for the exercising of stock options of \$69,225 and use of the Company's operating facility in the amount of \$85,43. The cash inflow for the nine months ended September 30, 2010 is a direct result of the February 26, 2010 private placement, which provided net proceeds of \$1,881,495 to the Company offset by the repayment of the credit facility the Company had in place with a financial institution last year of \$854,717.

The cash balance of the Company at September 30, 2011 was \$23,728, a decrease of \$460,729 from December 31, 2010. Current assets at September 30, 2011 were \$2,616,368 compared to \$2,044,222 at December 31, 2010. Working capital decreased by \$212,360 to a deficiency of \$852,571 as of September 30, 2011 from a deficiency of \$640,211 in working capital as of December 31, 2010.

The Company's current business plan and sales forecast projects revenue growth in 2011 and beyond. The Company believes that its success in securing a sales contract vehicle and/or growing sales with each of the U.S. Department of Homeland Security – Customs and Border Protection, the U.S. Navy, and the U.S. Fish and Wildlife Service will lead to growth within these departments and future opportunities within other departments in the U.S. government, and abroad with other governments.

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.

On an ongoing basis, the Company investigates various financing options, including a revolving credit facility and/or additional equity financings as well as other strategic funding sources to fund the continuing efforts to grow the use of 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. Growth capital is dependent upon the success of the Company and upon the state of the capital markets in general.

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 was 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 was required to maintain a current ratio in excess of 0.75:1.0 while any portion of the demand facility is outstanding. As at September 30, 2011 the Company had bank indebtedness of \$85,434 against its revolving demand operating facility and a current ratio of 0.73:1.0. This bank indebtedness was paid in full on October 5, 2011 with cash from operations and the credit facility was cancelled by Route1 Inc. As of the date of this MD&A the Company does not have any bank indebtedness.

The following table discloses future payments as at September 30, 2011 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	Total	No later than 1 year	Later than one year	
			and not later than five years	Later than five years
Severance liability	\$ 420,000	\$ 366,000	\$ 54,000	\$ -
Operating leases	2,509,000	160,000	1,204,000	1,145,000
	\$ 2,929,000	\$ 526,000	\$ 1,258,000	\$ 1,145,000

OFF-BALANCE SHEET ARRANGEMENTS

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

TRANSACTIONS WITH RELATED PARTIES

The Company has directors and officers which are considered related parties. The Company had the following transactions and/or outstanding amounts with related parties for the three and nine months ended September 30, 2011:

- The Company made payments (including HST) to 1220764 Ontario Inc. for management services provided by Mr. Tony P. Busseri, a director of the Company in the amount of \$101,700 in the three months ended September 30, 2011 and \$305,100 in the nine months ended September 30, 2011. The transaction was measured at the 'exchange amount' agreed upon by the parties.
- The Company made payments or incurred expense due to key management (Chief Technology Officer, Chief Operating Officer and Vice President of Finance and Administration in the three and nine months ended September 30, 2011 and twelve months ended December 31, 2010 as follows:

	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011	Twelve months Ended December 31, 2010
Short-term employee benefits	\$ 148,854	\$ 442,547	\$ 489,116
Stock option expense	114,068	381,631	394,737
	\$ 262,922	\$ 824,178	\$ 883,853

PROPOSED TRANSACTIONS

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

CRITICAL ACCOUNTING ESTIMATES

The condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, *Interim Financial Reporting*. These are the Corporation’s International Financial Reporting Standards (“IFRS”) interim condensed consolidated financial statements for part of the period covered by the first IFRS annual financial statements and IFRS 1, *First-time Adoption of International Financial Reporting Standards* has been applied. The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements. 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 IFRS. 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 device and the MobiKEY Fusion device) sales and subscription services (i.e. TruOFFICE application software). The Company recognizes revenue in accordance with IAS 18, “Revenue”.
- 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.

FUTURE ACCOUNTING POLICY CHANGES

Financial Instruments

The IASB has issued an amendment to IFRS 7, “Financial Instruments: Disclosures” (IFRS 7 amendment), requiring incremental disclosures regarding transfers of financial assets. This amendment is effective for annual periods beginning on or after July 1, 2011. The Company will apply this amendment at the beginning of its 2012 financial year. The Company does not expect the implementation to have any impact on the Company’s disclosures.

IFRS 9, “Financial Instruments” (“IFRS 9”) was issued by the IASB on November 12, 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.

- IFRS 9 requires all recognised financial assets that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods.
- The most significant effect of IFRS 9 regarding the classification and measurement of financial liabilities relates to the accounting for changes in fair value of a financial liability (designated as at fair value through profit or loss) attributable to changes in the credit risk of that liability. Specifically, under IFRS 9, for financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is recognised in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Previously, under IAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit or loss was recognised in profit or loss.

IFRS 9 is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted. The Company is currently evaluating the impact of IFRS 9 on its financial statements.

Consolidated Financial Statements

IFRS 10 *Consolidated Financial Statements*, effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. Management anticipates that this standard will be adopted in the Company’s consolidated financial statements for the period beginning January 1, 2013 and has not yet had an opportunity to consider the potential impact of the adoption of IFRS 10.

Joint Arrangements

IFRS 11 Joint Arrangements, effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. Management anticipates that this standard will be adopted in the Company's consolidated financial statements for the period beginning January 1, 2013 and has not yet had an opportunity to consider the potential impact of the adoption of IFRS 11.

Disclosure of Interests in Other Entities

IFRS 12 *Disclosure of Interests in Other Entities*, effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. Management anticipates that this standard will be adopted in the Company's consolidated financial statements for the period beginning January 1, 2013 and has not yet had an opportunity to consider the potential impact of the adoption of IFRS 12.

Fair Value Measurement

IFRS 13 *Fair Value Measurement* defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except for: share-based payment transactions within the scope of IFRS 2 *Share-based Payment*; leasing transactions within the scope of IAS 17 *Leases*; measurements that have some similarities to fair value but that are not fair value, such as net realizable value in IAS 2 *Inventories* or value in use in IAS 36 *Impairment of Assets*. This standard is effective for annual periods beginning on or after January 1, 2013, with early application permitted and management has not yet had an opportunity to consider the potential impact of the adoption of IFRS 13.

Related Party Disclosures

IAS 24 *Related Party Disclosures* (as revised in 2009) modifies the definition of a related party and simplifies disclosures for government-related entities. The disclosure exemptions introduced in IAS 24 (as revised in 2009) do not affect the Company because the Company is not a government-related entity. However, disclosures regarding related party transactions and balances in these consolidated financial statements may be affected when the revised version of the Standard is applied in future accounting periods because some counterparties that did not previously meet the definition of a related party may come within the scope of the Standard.

Deferred Taxes – Recovery of Underlying Assets

The IASB has issued an amendment to IAS 12, "Income Taxes" ("IAS 12 amendment"), which introduces an exception to the general measurement requirements of IAS 12 in respect of investment properties measured at fair value. The IAS 12 amendment is effective for annual periods beginning on or after January 1, 2012. The Company will apply the amendment at the beginning of its 2012 financial year. The Company has yet to assess the impact of the IAS 12 amendment on its results of operations, financial position and disclosures.

Presentation of Financial Statements

IAS 1 *Presentation of Financial Statements* was amended to improve the consistency and clarity of the presentation of items of other comprehensive income by adding the requirement to group items on the basis of whether they may be reclassified subsequently in profit or loss. Management anticipates that this standard will be adopted in the Company's consolidated financial statements for the period beginning July 1, 2012 and has not yet had an opportunity to consider the potential impact of the adoption of IAS 1.

Employee Benefits

IAS 19 *Employee Benefits* was amended to provide users with a clearer picture of the commitments resulting from defined benefit plans. Amendments include the elimination of the corridor approach, requirement to present gains and losses related to defined benefits plans in other comprehensive income, and the addition of disclosure requirements to better show the characteristics of the defined benefit plans and risks arising from those plans. Management anticipates that this standard will be adopted in the Company's consolidated financial statements for the period beginning January 1, 2013. The Company does not currently have defined benefit plans therefore adoption of IAS 19 will have no impact on the financial statements.

TRANSITION TO IFRS

The Company has adopted IFRS effective for interim and annual periods commencing January 1, 2011, including the preparation and reporting of one year of comparative figures. The opening balance sheet has been prepared as of January 1, 2010. Prior to the adoption of IFRS the Company prepared its financial statements in accordance with Canadian generally accepted accounting principles ("GAAP"). The Company's consolidated financial statements for the year ending December 31, 2011 will be the first annual financial statements that comply with IFRS.

1) Elected exemptions applied from full retrospective application

In preparing these consolidated financial statements in accordance with IFRS 1, "First-time adoption of International Reporting Standards" ("IFRS 1"), the Company has applied certain of the optional exemptions from full retrospective application of IFRS. The optional exemptions applied are as follows:

a) **Business Combinations (IFRS 3 2008)**

The Company was formed through a reverse takeover in 2004 which meets the definition of business combination under IFRS. The Company has applied the business combinations exemption in IFRS 1 to not apply IFRS 3 2008 retrospectively to past business combinations. Accordingly the Company has not restated business combinations that took place prior to the transition date.

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

The Company has elected to adopt under IFRS 1 the option to apply IFRS 2 retrospectively only to share-based options granted that are unvested as at transition date of January 1, 2010. The Company has stock option plans that qualify as share based payments under IFRS 2 granted to directors, officers, employees and consultants.

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

The Company elects to apply IAS 23 on a prospective basis from the date of transition of January 1, 2010.

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

The Company has no arrangements that are deemed as leases under, hence no impact of IFRIC 4. The only leasing arrangement the Company has is that of its premises. This is classified as an operating lease under IAS 17.

e) **Intangible assets (IAS 38)**

The Company values all of its intangible assets using the cost model and not the revaluation model that IFRS allows. System Computer Software is the only asset the Company currently classifies as an intangible asset and is amortized over 12 months hence the Company does not perform an impairment test on its intangible asset because the risk of impairment is insignificant. Computer Software for appliances will be amortized over 60 months and impairment valuation will be performed annually.

f) **Fair value or revaluation as deemed cost (IAS 16, 40 and 38) Property, Plant and Equipment.**

The Company has elected not to apply the IFRS 1 election and reset the deemed cost of assets to fair value on transition date but will retrospectively apply IAS 16. The Company has also elected to use the cost model method property, plant and equipment on transition date. This is generally consistent with GAAP treatment. PP&E will be recorded at cost, less depreciation and impairment. The Company currently does not have any Property or Plants or Investment property.

2) IFRS 1 Exemptions and Exceptions which are not applicable to the Company are as follows:

1. Employee benefits (IAS 19)
2. Cumulative translation differences (IAS 21)
3. Compound Financial Instruments (IAS 32 & 39)
4. Investments in subsidiaries, jointly controlled entities and associates (IAS 27 & IAS 31)
5. Insurance contracts (IFRS 4)
6. Decommissioning liabilities (IAS 37 and IAS 16)
7. Fair value measurement of financial assets or financial liabilities at initial recognition (IAS 39)
8. Service Concession agreements (IFRIC 12)
9. Transfer of assets from customers (IFRIC 18)

Mandatory exemptions to retrospective application

In preparing these consolidated financial statements in accordance with IFRS 1, the Company has applied certain full retrospective application of IFRS. The mandatory exemptions applied from full retrospective application of IFRS are as follows:

a) **Estimates**

Hindsight was not used to create or revise estimates and accordingly estimates previously made by the Company under GAAP are consistent with their application under IFRS.

IFRS 1 Mandatory Exemptions which are not applicable to the Company are as follows:

1. Derecognition of financial assets and financial liabilities
2. Hedge accounting
3. Non-Controlling Interests

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

a) Establishing Fair Value

The carrying amount of financial instruments including cash and cash equivalents accounts receivable, other receivables, notes receivable and accounts payable and other 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 June 30, 2011 and December 31, 2010:

	September 30, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
FINANCIAL ASSET				
Loans and receivables				
Cash and cash equivalents (i)	\$ 23,728	\$ 23,728	\$484,457	\$484,457
Accounts receivable (i)	\$ 1,052,572	\$ 1,052,572	\$475,302	\$475,302
Other receivables (i)	\$ 53,328	\$ 53,328	\$ 27,471	\$ 27,471
FINANCIAL LIABILITIES				
Other liabilities				
Bank Indebtedness	\$ 85,434	\$ 85,434	-	-
Accounts payable and other liabilities (i)	1,048,421	1,048,421	\$ 988,443	\$ 988,443

(i) The fair value of these instruments is 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 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 and cash equivalents	Yes		Yes	Yes
Accounts receivable	Yes		Yes	
Other receivables	Yes			
Accounts payable and other 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. As at September 30, 2011, the largest single customer represented approximately 33.4 % (a reseller with more than one customer) of recorded revenue.

Cash and cash equivalents

Cash and cash equivalents consist 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, 2011, the Company had cash consisting of cash on hand and deposits with banks of \$23,728 (December 31, 2010 - \$484,457). During the three months ended September 30, 2011, the Company did not hold any investments in asset-backed commercial

paper. At November 21, 2011, the Company had cash consisting of cash on hand and deposits with banks of \$355,903.

Accounts receivable

Accounts receivable consist 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 is 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. As at September 30, 2011 the Company had fully written-off prior year allowances of invoices. At September 30, 2011, the largest single customer’s accounts receivable represented approximately 58.3% (September 30, 2010 – 45.3%) of the total accounts receivable. Subsequent to September 30, 2011 all of the outstanding accounts receivable as at September 30, 2011 was paid in full.

Bank indebtedness

Bank indebtedness consists of cash owing to a financial institution for the use of the revolving credit facility. At September 30, 2011, the Company had bank indebtedness of \$85,434 (December 31, 2010 - \$nil). The Company fully paid this bank indebtedness on October 5, 2011.

The following table outlines the details of the aging of the Company’s receivables as at September 30, 2011 and December 31, 2010:

	September 30, 2011	December 31, 2010
Current	\$ 311,549	\$ 17,160
Past due		
1 – 60 days	741,023	254,673
Greater than 60 days	-	203,469
Less: Allowance for doubtful accounts	-	-
Total accounts receivable, net	<u>\$ 1,052,572</u>	<u>\$ 475,302</u>

The following table outlines the details of the Allowance for Doubtful Accounts of the Company's receivables as at September 30, 2011 and December 31, 2010:

	September 30, 2011	December 31, 2010
Opening balance in period	\$ -	\$ (18,460)
Collected in period	-	-
Write-off in period	-	18,460
Closing balance in period	\$ -	\$ -

(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, which by nature, are due predominately from government agencies with a high level of certainty of collection.

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, 2011:

	2011	2012	2013 and beyond	Total
Accounts payable and other liabilities	\$ 895,088	\$ 153,333	\$ -	\$ 1,048,421
Operating lease commitments	-	215,806	2,293,458	2,509,264
	\$ 895,088	\$ 369,139	\$ 2,293,458	\$ 3,557,685

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, 2011, the Company had non Canadian dollar net monetary liabilities of approximately US\$7,350 and €2,842 (December 31, 2010 - approximately US\$4,609 and €nil). Any changes in the respective exchange rates as at September 30, 2011 would have resulted in non-material exchange gains or losses 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, 2011, cash totalled \$23,728 (December 31, 2010 - \$484,457).

OTHER MD&A REQUIREMENTS

Disclosure of Outstanding Share Data

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

- 388,920,615 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
- 32,815,000 common share purchase options (“**Options**”) convertible into 32,815,000 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
 - 1,500,000 Options issued on September 15, 2010 at \$0.20/share expiring September 15, 2015
 - 250,000 Options issued on November 18, 2010 at \$0.275/share expiring November 18, 2015
 - 650,000 Options issued on December 16, 2010 at \$0.275/share expiring December 16, 2015
 - 2,725,000 Options issued March 24, 2010 at \$0.13/share expiring March 24, 2015 were forfeited.
 - 250,000 Options issued on May 19, 2010 at \$0.13/share expiring on May 19, 2015 were forfeited.
 - 50,000 Options issued on August 24, 2010 at \$0.15/share expiring on August 24, 2015 were forfeited.
 - 250,000 Options issued on November 18, 2010 at \$0.275/share expiring on November 18, 2015 were forfeited.
 - 4,000,000 Options issued March 24, 2010 at \$0.13/share expiring March 24, 2015 were forfeited.
 - 2,500,000 Options issued on February 28, 2011 at \$0.25/share expiring February 28, 2016
 - 390,000 Options issued March 24, 2010 at \$0.13/share expiring on March 24, 2015 were converted to shares.
 - 245,000 Options issued March 24, 2010 at \$0.13/share expiring on March 24, 2015 were forfeited.
 - 100,000 Options issued on May 25, 2011 at \$0.25/share expiring May 25, 2016
 - 75,000 Options issued on May 25, 2011 at \$0.25/share expiring May 25, 2016 were forfeited.
 - 52,500 Options issued on May 19, 2010 at \$0.13/share expiring May 19, 2015 were forfeited.
 - 22,500 Options issued May 19, 2010 at \$0.13/share expiring on May 19, 2015 were converted to shares.
 - 120,000 Options issued March 24, 2010 at \$0.13/share expiring on March 24, 2015 were converted to shares.
 - 625,000 fully vested Options issued August 22, 2011 at \$0.16/share expiring on August 22, 2016.

- 200,000 Options issued on August 25, 2011 at \$0.25/share expiring August 25, 2016
- 100,000 Options issued on August 25, 2011 at \$0.25/share expiring August 25, 2016 were forfeited.
- 50,000 Options issued on August 24, 2010 at \$0.15/share expiring August 24, 2015 were forfeited.

Risk Factors and Uncertainty

The Company’s risk factors are substantially unchanged from and should be read in conjunction with Route1 Inc.’s Annual MD&A dated March 23, 2011, for the year ended December 31, 2010.

Audit Committee

The two members of the Audit Committee are independent and all meet the qualifications of a financial expert and all are financially literate as such term is defined in National Instrument 52-110 - Audit Committees.

Legal proceedings

In the normal course of operations, the Company may be subject to litigation claims from customers, suppliers, patent holders, resellers and former employees. A provision is recognized when the probability that the event will occur is greater than the probability that it will not. The Company regularly reviews any outstanding claims to see if they meet the criteria. A provision is calculated based on management’s best estimate of probable outflow of economic resources.

REVENUE INFORMATION

The Company is organized and managed as a single reportable business entity with two distinct revenue streams, being devices and appliances, and services. The Company considers revenue realizable and earned when the product has been delivered or the services have been provided to the customer and collectability is reasonably assured. For sale of devices, revenue is recognized at the time of shipment of the device which constitutes transfer of ownership of the device. Revenue for the services component is reported as deferred revenue on the balance sheet and is recognized as earned revenue in the period which the service is provided. At September 30, 2011, the Company had \$2,068,233 (December 31, 2010 - \$1,722,141) in deferred revenue.

The following table provides a component presentation of the Company’s revenue stream for the three months ended September 30, 2011 and 2010:

	2011		2010	
	Revenue	% of Total	Revenue	% of Total
Devices	\$ 173,062	12.4	\$ 385,665	27.9
Services	1,226,101	87.6	995,082	72.1
	\$ 1,399,163	100.0	\$ 1,380,747	100.0

For the three months ended September 30, 2011, a reseller selling the Company’s Devices and Services to their multiple customers accounted for 33.4% of the Company’s revenue stream.

The following table provides a component presentation of the Company's revenue stream for the nine months ended September 30, 2011 and 2010:

	2011		2010	
	Revenue	% of Total	Revenue	% of Total
Devices	\$ 463,734	11.4	\$ 644,111	17.9
Services	3,591,023	88.6	2,949,086	82.1
	\$ 4,054,757	100.0	\$ 3,593,197	100.0

For the nine months ended September 30, 2011, a reseller selling the Company's Devices and Services to their multiple customers accounted for 31.6% of the Company's revenue stream.

The following table provides a geographical presentation of the Company's revenue stream for the three months ended September 30, 2011 and 2010:

	2011		2010	
	Revenue	% of Total	Revenue	% of Total
USA	\$ 979,746	70.0	\$ 940,957	68.1
Europe	279,860	20.0	307,946	22.3
Canada	139,557	10.0	131,844	9.6
	\$ 1,238,405	100.0	\$ 1,206,996	100.0

The following table provides a geographical presentation of the Company's revenue stream for the nine months ended September 30, 2011 and 2010:

	2011		2010	
	Revenue	% of Total	Revenue	% of Total
USA	\$ 2,762,683	68.1	\$ 2,212,684	61.6
Europe	833,060	20.5	974,006	27.1
Canada	459,014	11.4	406,507	11.3
	\$ 4,054,757	100.0	\$ 3,593,197	100.0

SEVERENCE CHARGES

Severance charges for the three months ended September 30, 2011 were \$260,953 (2010- \$460,000) and were a one-time expense the Company incurred to terminate the employment agreement of the Company's former Chief Technology Officer. Payment of this liability will be made on a monthly payment schedule and the liability will be fully discharged by January 31, 2013.

Severance charges for the three months ended September 30, 2010 were \$460,000 (2009- \$nil) and were 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 had been recorded with both its short term (\$230,000) and long term components (\$210,833). Payment of this liability will be made on a bi-monthly payment schedule and the liability will be fully discharged by August 31, 2012.

SUBSEQUENT EVENTS

- On October 4, 2011, the Company entered into a \$550,000 (December 31 2010 - \$500,000) credit facility with a different banking and financial services organization consisting of a \$500,000 revolving demand operating facility and a \$50,000 VISA facility. The revolving demand credit facility will carry an interest rate equal to the lender's prime rate of interest plus 1.80%. The credit facility will be secured by the assets of the Company. No margining is required for outstanding amounts up to \$100,000; accessing an amount in excess of \$100,000 shall be based on the balance and term of the Company's trade accounts receivables outstanding plus the amount of SR&ED tax credits filed and refundable. 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 and a Funded Debt to EBITDA (calculated on a yearly basis) of not greater than 2.50:1.
- On October 19, 2011, the Company announced it has been named to the prestigious Deloitte Technology Fast 50™, a ranking of the 50 fastest growing technology companies in Canada, based on the percentage of revenue growth over five years. Route1 is ranked #26 this year, with an increase in revenues of 903 percent from 2006 to 2010.
- On November 23, 2011, Amar S. Doman tendered his resignation from the Company's Board of Directors.

RECONCILIATION AS REPORTED UNDER CANADIAN GAAP AND IFRS

Reconciliation of equity (deficiency) as reported under Canadian GAAP and IFRS

The following is a reconciliation of the Company's total equity reported in accordance with Canadian GAAP to its equity (deficiency) in accordance with IFRS at the transition date:

	Footnote	Share Capital	Warrants	Contributed Surplus	Deficit	Total Equity
As reported under GAAP – December 31, 2009		\$23,977,296	\$2,949,072	\$5,702,410	\$(34,208,879)	\$(1,580,101)
Differences increasing (decreasing) reported amount:						
IFRS Adjustment	(a)			7,937	(7,937)	-
As reported under IFRS - Jan 1, 2010		\$23,977,296	\$2,949,072	\$5,710,347	\$(34,206,816)	\$(1,580,101)

The following is a reconciliation of the Company's total equity reported in accordance with Canadian GAAP to its equity (deficiency) in accordance with IFRS at September 30, 2010:

	Footnote	Share Capital	Warrants	Contributed Surplus	Deficit	Total Equity
As reported under GAAP – September 30, 2010		\$24,112,764	\$1,746,027	\$9,219,027	\$(36,057,132)	\$(979,314)
Differences increasing (decreasing) reported amount:						
IFRS Adjustment	(a)			264,529	(264,529)	-
As reported under IFRS - September 30, 2010		\$24,112,764	\$1,746,027	\$9,483,556	\$(36,321,661)	\$(979,314)

The following is a reconciliation of the Company's total equity reported in accordance with Canadian GAAP to its equity (deficiency) in accordance with IFRS at December 31, 2010:

	Footnote	Share Capital	Warrants	Contributed Surplus	Deficit	Total Equity
As reported under GAAP – December 31, 2010		\$24,112,764	\$1,746,027	\$ 9,515,715	\$(35,966,949)	\$(592,403)
Differences increasing (decreasing) reported amount:						
IFRS Adjustment	(a)			345,109	(345,109)	-
As reported under IFRS – December 31, 2010		\$24,112,764	\$1,746,027	\$ 9,860,864	\$(36,312,058)	\$(592,403)

(a) Under IFRS 2 all unvested options of each installment were recognized as compensation expense based on a graded vesting method net of a forfeiture estimate as compared to the straight-line method expensed under GAAP. As well, under IFRS 2 the Company expenses the vesting periods according to granted terms of 30% in year 1, 30% in year 2 and 40% in year 3 whereas under GAAP vesting had to be expensed at three equal vesting portions or 33.33% for each year. In addition, the Company retrospectively adjusted for share-based options granted to “consultants” under GAAP as “others providing similar service as employees” allowable under IFRS 2 if certain conditions were met.

Reconciliation of Comprehensive loss as reported under Canadian GAAP and IFRS

The following is a reconciliation of the Company's Comprehensive loss reported in accordance with Canadian GAAP to its Comprehensive loss in accordance with IFRS at December 31, 2010:

	Three months ended September 30, 2010	Six months ended September 30, 2010	Year ended December 31, 2010
As reported under GAAP	(1,057,655)	(1,848,253)	(1,758,070)
IFRS adjustment	(101,123)	(256,592)	(337,172)
As reported under IFRS	(1,158,778)	(2,104,845)	(2,095,242)

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 8 King Street East, Suite 600, Toronto, Ontario, Canada M5C 1B5 (telephone 416-848-8391).