

JEMTEC INC.

Interim Financial Statements January 31, 2006

Notice to Reader:

The accompanying interim financial statements of JEMTEC Inc. for the three and six month periods ended January 31, 2006 have been prepared by and are the responsibility of the Company's management. These statements are unaudited and have not been reviewed by independent auditors.

JEMTEC INC.

Balance Sheets

January 31, 2006 July 31, 2005

ASSETS

Current

Cash and cash equivalents	\$ 1,858,102	\$ 1,699,756
Accounts receivable	258,316	473,293
Prepaid expenses and deposits	72,067	1,500

Total current assets 2,188,485 2,174,549

Property and equipment (note 4) 341,289 365,122

Future income taxes 36,775 41,947

Total assets \$ 2,566,549 \$ 2,581,618

LIABILITIES

Current

Accounts payable and accrued liabilities	\$ 257,922	\$ 279,105
Deferred revenue	8,153	23,115
Current portion of capital lease obligation (note 5)	73,184	81,093
Income taxes payable	102,368	409,743

Total current liabilities 441,627 793,056

Capital lease obligation (note 5) 202,373 238,922

Total liabilities 644,000 1,031,978

SHAREHOLDERS' EQUITY

Share capital (note 7)	1,247,160	1,247,160
Contributed surplus	139,756	24,612
Retained earnings	535,633	277,868

Total shareholders' equity 1,922,549 1,549,640

Total liabilities and shareholders' equity \$ 2,566,549 \$ 2,581,618

The accompanying notes are an integral part of these unaudited financial statements

Approved by the Board of Directors:

"Eric Caton"
Director

"Leslie Markow"
Director

JEMTEC INC.

Statements of Operations and Retained Earnings

	For the three month period ended January 31,		For the six month period ended January 31,	
	2006	2005	2006	2005
Revenue				
Leasing, monitoring and activation (note 8)	\$ 646,101	\$ 636,660	\$ 1,313,455	\$ 1,265,636
Parts, sales and other	23,869	62	24,494	1,733
	<u>669,970</u>	<u>636,722</u>	<u>1,337,949</u>	<u>1,267,369</u>
Expenses				
Salaries and benefits	54,338	56,256	110,260	113,200
Amortization	16,094	17,963	31,878	22,292
Repairs and maintenance (recovery)	5,319	(14,043)	16,355	18,709
Monitoring and activation fees	128,858	92,243	256,841	169,262
Equipment rent and installation	54,973	43,157	106,731	63,477
Consulting fees	47,716	27,000	82,716	55,036
Travel	10,288	5,680	23,223	17,892
Shareholder communications	24,033	12,273	25,614	13,668
Professional fees	22,572	5,062	26,582	7,012
Office	31,109	29,511	62,978	52,234
Interest on capital leases	5,164	7,602	10,754	8,274
Other interest expenses	571	1,182	571	1,348
Stock-based compensation	57,572	4,715	115,144	4,715
Directors' fees	19,500	18,500	27,000	24,000
Accounting and administrative fees	15,055	5,500	23,942	11,500
	<u>493,162</u>	<u>312,601</u>	<u>920,589</u>	<u>582,619</u>
Income before income taxes	176,808	324,121	417,360	684,750
Income tax expense				
Current	66,375	241,524	154,423	241,524
Future	2,586	4,986	5,172	4,986
	<u>68,961</u>	<u>246,510</u>	<u>159,595</u>	<u>246,510</u>
Net income for the period	107,847	77,611	257,765	438,240
Retained earnings (deficit) - Beginning of period	427,786	(76,028)	277,868	(436,657)
Retained earnings (deficit) - End of period	\$ 535,633	\$ 1,583	\$ 535,633	\$ 1,583
Earnings per share:				
Basic	\$ 0.05	\$ 0.04	\$ 0.11	\$ 0.21
Diluted	\$ 0.04	\$ 0.03	\$ 0.11	\$ 0.19
Weighted average number of shares outstanding:				
Basic	2,355,943	2,071,659	2,355,943	2,071,659
Diluted	2,449,133	2,301,288	2,443,205	2,297,412

The accompanying notes are an integral part of these unaudited financial statements

JEMTEC INC.

Statements of Cash Flows

	For the three month period ended January 31,		For the six month period ended January 31,	
	2006	2005	2006	2005
Cash flows from (used in) operating activities				
Net income for the period	107,847	77,611	257,765	438,240
Adjustments to reconcile net income to net cash used in operating activities:				
- amortization	16,094	17,963	31,878	22,292
- stock-based compensation	57,572	4,715	115,144	4,715
- future income taxes	2,586	4,986	5,172	4,986
Changes in non-cash working capital:				
- accounts receivable	26,037	(22,184)	214,977	(241,523)
- prepaid expenses	(70,567)	877	(70,567)	2,089
- accounts payable and accrued liabilities	(10,572)	20,398	(21,183)	1,565
- deferred revenue	(4,546)	(4,485)	(14,962)	1,843
- due to related parties	15,000	15,000	-	(39,250)
- income taxes payable	(19,462)	138,041	(307,375)	138,041
Cash flows - operating activities	119,989	252,922	210,849	332,998
Cash flows used in investing activities				
Purchase of property and equipment	(4,706)	-	(8,045)	-
Cash flows - investing activities	(4,706)	-	(8,045)	-
Cash flows from (used in) financing activities				
Payment on capital lease obligation	(19,969)	(35,112)	(44,458)	(41,858)
Cash flows - financing activities	(19,969)	(35,112)	(44,458)	(41,858)
Net increase in cash	95,314	217,810	158,347	291,140
Cash, beginning of period	1,762,788	771,328	1,699,756	697,998
Cash, end of period	1,858,102	989,138	1,858,103	989,138

The accompanying notes are an integral part of these unaudited financial statements

Supplemental cash disclosures**Cash paid for:**

Income taxes	\$ 85,932	\$ -	\$ 461,893	\$ -
Interest	\$ 5,735	\$ 8,950	\$ 11,324	\$ 9,622

1. Nature of Operations

The Company's core business is the provision of services and technology for offender monitoring in Canadian federal and provincial correctional departments.

2. Significant Accounting Policies

a) General

These financial statements have been prepared in Canadian dollars and in accordance with Canadian generally accepted accounting principles.

b) Use of estimates

The preparation of these financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the revenues and expenses during the reporting periods, in addition to the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements. Actual results could differ from those estimates.

c) Currency and foreign exchange

The functional currency of the company is the Canadian dollar. Monetary assets and liabilities denominated in another currency are translated at exchange rates in effect at the balance sheet dates. Other non-monetary balance sheet items denominated in another currency are translated at the rates of exchange in effect at the time the items arose. Revenue and expenses are translated at the exchange rates in effect at the time of the transaction. Gains and losses arising from fluctuations in exchange rates are included in operations for the periods in which they occur.

d) Cash and cash equivalents

Cash and cash equivalents are defined as cash on hand and short term, highly liquid money market instruments with original maturities of three months or less.

e) Property and equipment

Property and equipment are stated at cost less accumulated amortization. Amortization is charged to earnings over the estimated useful lives of the respective assets at the following rates:

Furniture & fixtures	20% declining balance
Monitoring equipment	straight-line over 5 years or contract period

Expenditures for maintenance and repairs that do not improve or extend the life of the assets are expensed as operations, while major repairs are capitalized.

2. Significant Accounting Policies (continued)

f) Asset impairment

On an annual basis, or when impairment arises, the Company evaluates the future recoverability of its property and equipment. Impairment losses or write-downs are recorded in the event the net book value of such assets exceeds the estimated future cash flows attributable to such assets.

g) Revenue recognition

Rental and monitoring income is recognized pursuant to various lease agreements which specify the terms and conditions of rental and the services to be performed and electronic surveillance. Rental income is recognized on a straight-line basis over the terms of the leases. Revenue from the sale of parts which are required to repair and maintain the monitoring equipment is recognized upon delivery to the lessee. Maintenance and monitoring service income is recognized when the services are performed.

The Company recognizes sales and leasing revenue over the term of the applicable operating services agreements. The term of existing service agreements is between three and five years. Generally, the lessees have the option to renew or cancel the lease and service agreements upon the expiration of each lease term or, in certain circumstances, the agreements may be cancelled upon specific notice provided to the Company. In situations where leases are terminated, the leased monitoring equipment would be returned to the Company or the Company's lessors with no further obligation on behalf of the lessee.

h) Stock-based compensation

The Company follows the recommendations of CICA Handbook Section 3870 "*Stock-based Compensation and Other Stock-based Payments*" which establishes standards for the recognition, measurement and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services. Effective for year ends beginning on or after January 1, 2004, these recommendation require that compensation for all awards made, including stock appreciation rights, direct awards of stock and awards that call for settlement in cash or other assets, be measured and recorded in the financial statements at fair value. For the purpose of this Section, employees include directors who receive stock compensation for services provided as director. This Section also sets out fair value based methods of accounting for stock options issued to employees.

For the years ended July 31, 2002 and 2003, no compensation expense was recognized for stock options granted to employees and directors, as the company was using the intrinsic method to account for the stock option grants. During the year ended July 31, 2004, the Company adopted, on a prospective basis, the fair value based method of accounting for stock based compensation for all grants of options to employees, non-employees and directors in accordance with the prospective application provision of Section 3870. All option grants beginning August 1, 2003 are accounted by using the fair value based method, and stock based compensation expense is computed the Black-Scholes option pricing model. Accordingly, the fair value of the stock options at the date of grant is charged to operations on a straight-line basis over the vesting period. Any consideration paid on exercise of stock options together with the related portion previously recognized as stock based compensation is credited to share capital.

2. Significant Accounting Policies (continued)

i) Earnings per share

Basic earnings per share is computed by dividing earnings (loss) for the period by the weighted average number of common shares outstanding during the period. Diluted earnings per share has been calculated using the treasury stock method. This method assumes that common shares are issued for the exercise of warrants and options and that the assumed proceeds from the exercise of warrants and options are used to purchase common shares at the average market price during the period. The difference between the number of shares assumed issued and the number of shares assumed purchased is then added to the basic weighted average number of shares outstanding to determine the fully diluted number of common shares outstanding. No exercise or conversion is assumed during periods in which a net loss is incurred as the effect is anti-dilutive.

j) Income taxes

The Company uses the asset and liability method of accounting for income taxes whereby future income tax assets are recognized for deductible temporary differences and operating loss carry-forwards, and future income tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the amounts of assets and liabilities recorded for income tax and financial reporting purposes. Future income tax assets are recognized only to the extent that management determines that it is more likely than not that the future income tax assets will be realized. Future income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment or substantive enactment. The income tax expense or benefit is the income tax payable or refundable for the period plus or minus the change in future income tax assets and liabilities during the period.

3. Financial Instruments

The Company's financial instruments recognized in the balance sheet consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, bank loan, due to related parties, income taxes payable, and capital lease obligations. The fair values of these instruments approximates their carrying value due to their short-term maturity or, in the case of the capital lease obligation, the rate implicit in the lease arrangements.

a) Credit risk

The Company's principal business activities are located in Canada. The Company performs certain credit evaluation procedures and does not require collateral for financial instruments subject to credit risk. The Company believes that credit risk is limited because the company routinely assesses the financial strength of its customers, and based upon factors surrounding the credit risk of its customers, establishes an allowance for uncollectible accounts and, as a consequence, believes that its account receivable credit risk beyond such allowances is limited.

3. Financial Instruments (continued)

The Company maintains cash deposits with financial institutions, which from time to time may exceed federally insured limits. The Company has not experienced any losses and believes it is not exposed to any significant credit risk from cash. At January 31, 2006, the Company had cash balances on deposit that exceeded federally insured limits by \$1,358,102. All of these funds are on deposit with a Schedule A bank in Canada.

b) Fair value

Unless otherwise noted, cash, accounts, advances and deposits receivable, loans and accounts payable are stated at amounts that approximate fair value.

c) Foreign exchange risk

The Company may be subject to limited currency risk due to the fluctuations of exchange rates amongst the Canadian and U.S. dollars.

d) Liquidity risk

The Company is exposed to liquidity risk as its continued operations are dependent upon the Company realizing its account receivable to satisfy its liabilities as they become due.

4. Property and Equipment

	January 31, 2006			July 31, 2005		
	Cost	Accumulated Amortization	Net Book Value	Costs	Accumulated Amortization	Net Book Value
Furniture and fixtures	\$ 39,978	\$ 34,611	\$ 5,367	\$ 35,676	\$ 34,074	\$ 1,602
Monitoring equipment	457,177	121,255	335,922	453,434	89,914	363,520
	<u>\$ 497,155</u>	<u>\$ 155,866</u>	<u>\$ 341,289</u>	<u>\$ 489,110</u>	<u>\$ 123,988</u>	<u>\$ 365,122</u>

Included in monitoring equipment are assets under capital lease at a cost of \$453,434 (July 31, 2005 - \$453,434) and a net book value of \$332,241 (July 31, 2005 - \$363,520).

The Company amortizes its monitoring equipment over its estimated useful life as described in note 2. Such estimates are based on management's experience and expectations of the continued renewal of the contracts for which equipment is acquired or the use of existing equipment in new contracts. Advances in technology and other considerations could result in significant changes to the estimated lives of these assets or otherwise impact the ability of the Company to realize on existing monitoring equipment. In these circumstances, additional provisions could be required.

5. Capital Lease Obligation

Further minimum lease payments to capital leases are as follows:

		Principal	Imputed Interest	Total
Year ending July 31,	2006	\$ 35,954	\$ 9,369	\$ 45,323
	2007	75,788	14,857	90,645
	2008	81,300	9,344	90,644
	2009	82,515	2,955	85,470
	2010	-	-	-
		<u>275,557</u>	<u>36,525</u>	\$312,082
Less: amounts representing interest (8%)				<u>(36,525)</u>
Present value of minimum lease payments				275,557
Less: current portion				<u>(73,184)</u>
				<u>\$202,373</u>

A general security agreement over all of the assets of the Company has been pledged as security for the capital lease obligations.

6. Bank Credit Facility and Loan Agreement

The Company has arranged an uncommitted term operating loan which is available to a maximum amount of \$75,000. The loan, if committed, would be due on demand, would bear interest at bank prime plus 1.3% per annum and would be secured by a general security agreement over all of the assets of the Company.

7. Share Capital

a) Authorized

Common shares:	Unlimited, no par value
First preference shares:	Unlimited, no par value, issuable in series
Second preference shares:	25,000 Series A, \$0.60 non-cumulative and redeemable

b) Issued and allotted

	Number of Common Shares	Amount
Balance July 31, 2004 and 2003	2,071,659	\$1,112,993
Shares issued for exercise of stock options	<u>284,284</u>	<u>\$ 134,167</u>
Balance July 31, 2005 and January 31, 2006	<u>2,355,943</u>	<u>\$1,247,160</u>

7. Share Capital (continued)

c) Options

During the year ended July 31, 2003, the Company adopted a fixed stock option plan that permits the directors of the company to grant incentive stock options to employees, directors and consultants to the Company. The maximum number of shares issuable under the plan, which follows the policies of the TSX Venture Exchange ("TSXV") regarding stock option awards, was 414,332. In January 2006, the Company amended its stock option plan to increase the number of shares reserved for issuance under the plan to 471,188. Options granted under the plan vest in 6 equal installments over a period of 18 months, with the first installment vesting immediately, and the remaining options vesting upon 6, 9, 12, 15 and 18 months after the date of grant. The option exercise price is generally set as the market price at the time of grant; however, a discount from the market price is permitted under the plan, subject to the policies of the TSX Venture Exchange.

The table below summarizes the options that have been granted under the Company's stock option plan.

	Number of Options	Weighted Average Exercise Price
Outstanding, July 31, 2004 and 2003	300,000	\$ 0.21
Granted	330,000	\$ 0.86
Exercised	<u>(284,284)</u>	\$ 0.33
Outstanding, July 31, 2005 and January 31, 2006	<u>345,716</u>	<u>\$ 0.84</u>

Prior to August 1, 2003, the Company applied the intrinsic value based method of accounting for stock based compensation granted under the Company's fixed stock option plan to employees and directors.

The fair value of the options granted in the fiscal year ended July 31, 2005 was estimated on the date of grant using the Black-Scholes option pricing model, assuming risk-free interest rates of 3.96%; dividend yield of \$nil; expected lives of 5 years and volatility of 122%.

During the year ended July 31, 2005, the Company granted 330,000 stock options. The fair value of the options granted is charged to earnings over the vesting period of 18 months. During the year ended July 31, 2005, 284,284 options were exercised, for net proceeds of \$93,712. Stock-based compensation expense of \$65,067 resulted and, of this amount, \$40,455 was credited to share capital upon the exercise of previously vested stock options and \$24,612 was credited to contributed surplus.

During the three and six month periods ended January 31, 2006, stock-based compensation expense was credited to contributed surplus in the amount of \$57,572 and \$115,144, respectively.

7. Share Capital (continued)

Options outstanding at January 31, 2006 are as follows:

	# of Options Granted	Expiry	Exercise Price	Number Outstanding as at January 31, 2006	Options Outstanding		Options Exercisable	
					Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Vested as at January 31, 2006	Weighted Average Exercise Price
Granted, February 26, 2003	150,000	8-Feb-08	\$ 0.11	50,000	0.29	\$ 0.02	50,000	\$ 0.03
Granted, September 21, 2004	50,000	21-Sep-09	\$ 0.30	50,000	0.53	\$ 0.04	50,000	\$ 0.07
Granted, June 9, 2005	<u>280,000</u>	23-Jun-10	\$ 1.10	<u>245,716</u>	3.12	\$ 0.78	<u>105,716</u>	\$ 0.57
	<u>480,000</u>			<u>345,716</u>	3.94 years	\$ 0.84	<u>205,716</u>	\$ 0.67

8. Economic Dependence

The Company presently derives substantially all of its revenue from two customers of which one customer contributed approximately 92% of revenue in the six month period ended January 31, 2006 (2005 - 92%). These contracts are reviewed periodically and have cancellation provisions. The non-renewal or cancellation of one or more of these contracts would have a material adverse impact on the Company.

Also, the Company is the exclusive Canadian distributor of Pro-Tech Monitoring, Inc.'s ("Pro-Tech") and BI Inc.'s (both U.S. companies) offender monitoring and tracking devices, the sales and leasing of which account for substantially all of the Company's revenues, capital asset additions and replacement parts purchased. The Company is economically dependent on Pro-Tech and BI Inc. for the continued supply of monitoring equipment, replacement parts, and maintenance services provided by Pro-Tech and BI Inc. for resale or rental by the Company.

9. Related Party Balances and Transactions

During the six month period ended January 31, 2006, \$0 (2005 - \$19,750) was paid to a director who is the President of the Company as an incentive bonus. During the six month period ended January 31, 2006, \$12,000 (2005 - \$24,000) was paid to the directors of the Company as directors fees, and an additional \$15,000 was accrued.

10. Earnings per Share

The following table shows the effect of dilutive securities on the weighted average common share outstanding. No adjustments to earnings were required for the calculation of diluted earnings per share.

	Three month period ended January 31,		Six month period ended January 31,	
	2006	2005	2006	2005
	Number of shares			
Basic weighted average shares outstanding	2,355,943	2,071,659	2,355,943	2,071,659
Effect of dilutive securities:				
Options	<u>93,190</u>	<u>229,629</u>	<u>87,262</u>	<u>225,753</u>
Diluted weighted average shares outstanding	<u>2,449,133</u>	<u>2,301,288</u>	<u>2,443,205</u>	<u>2,297,412</u>