

MANAGEMENT'S DISCUSSION AND ANALYSIS

Second Quarter, 2008

This Management's Discussion and Analysis ("MD&A") explains the financial condition and results of operations of Atlantis Systems Corp. ("the Company" or "we" or "our" or "us" or "ASC") as at and for the three months and six months ended June 30, 2008 with comparisons to the three months and six months ended June 30, 2007 and the year ended December 31, 2007, where applicable. This MD&A is intended to assist shareholders and other readers to understand our business and the key factors underlying our financial results. This MD&A should be read in conjunction with our unaudited Consolidated Financial Statements and the accompanying notes as at and for the three months and six months ended June 30, 2008 and 2007 and the audited annual consolidated financial statements, including the notes, for the year ended December 31, 2007. We prepare our consolidated financial statements in accordance with Canadian generally accepted accounting principles ("GAAP"). All amounts are stated in thousands of Canadian dollars except where otherwise noted. All tabular amounts are expressed in thousands of Canadian dollars except per share amounts. This MD&A is based on information available as at August 14, 2008 except where otherwise noted.

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GLOSSARY OF TECHNICAL TERMS AND OTHER INFORMATION

Certain technical terms used in this Management Discussion and Analysis are defined as follows:

“ASA” means Atlantis Systems America, Inc.

“ASC” means Atlantis Systems Corp.

“ASE” means Atlantis Systems Eduplus, a separate division of ASC.

“ASI” means Atlantis Systems International Inc.

“CF” means Canadian Forces.

“CFTS” means contracted flying training and support.

“CPT” means cockpit procedures trainer.

“DND” means Canadian Department of National Defence.

“EBITDA” means consolidated net income before interest, taxes, depreciation, amortization and non-cash charges and expenses other than accruals made in the normal course of business less any dividends on capital distribution.

“GAAP” means Canadian generally accepted accounting principles.

“HVTT” means helicopter virtual task trainer.

“IMTS” means integrated maintenance training system.

“PWU” means Power Workers’ Union

“PWUTI” means Power Workers’ Union Training Inc.

“RDAF” means Royal Danish Air Force.

“SMHP” means Sikorsky Maritime Helicopter Program.

All figures are in Canadian dollars unless otherwise stated.

All dollar values are in thousands of dollars unless otherwise stated.

All non dollar values are as stated.

1. HIGHLIGHTS

- Revenue for the three months ended June 30, 2008 was \$4.2 million, a reduction of \$0.1 million from the \$4.3 million recognized in the first quarter of 2008, a 72.4% decrease from the \$15.2 million reported for the same quarter in the previous year.
- We recorded a loss of \$2.3 million in the second quarter of 2008. This compared to a loss for the first quarter of 2008 of \$2.3 million and a profit of \$2.7 million for the second quarter of 2007.
- Effective April 30, 2008, we entered into financing arrangements with ComVest Capital, LLC (“ComVest”) that provided up to US\$6.6 million of financing in the form of a secured term loan in the amount of US\$2.6 million at a rate of interest of 12.5% per annum payable monthly and a deferred interest fee of 5% per annum payable at maturity as well as a secured revolving line of credit of up to US\$4.0 million based on a borrowing base at a rate of interest of US prime plus 2% per annum with a floor of 8%. The term loan matures on April 30, 2011 and the Line of Credit will be available until April 30, 2010, subject to a one-year extension at the option of the Company. These financing arrangements closed May 5, 2008 and the new term loan was used to repay the old term loan with the bank. The arrangement also involved the Company issuing warrants, with an expiry date of April 30, 2013, to acquire an aggregate of 9,300,000 common shares at an exercise price of \$0.09 per share. As at June 30, 2008, the Company was out of covenant on its rolling 6-month EBITDA covenant. ComVest agreed to waive the covenant for this period. The Company expects to have further discussions with ComVest on future covenant requirements. These discussions have not been finalized and it is likely that the covenant will be breached at the next compliance date. As a result the term debt has been reclassified as short term debt on the balance sheet.
- Our order backlog at June 30, 2008 was \$32.1 million, which includes approximately \$17.8 million for the CFTS support services to be recognized over the twenty year contract period, and \$7.7 million for Eduplus contracts. Our order backlog at March 31, 2008 was \$34.8 million, which included approximately \$18.0 million for the CFTS support services.
- We achieved a major milestone in our energy strategy by completing a joint venture agreement with the PWU Training Incorporated (PWUTI), a wholly owned subsidiary of the Power Workers’ Union, to create a new company called Powertrain Inc. (Powertrain), focused on becoming a “Centre of Excellence” in training for the global energy sector. Powertrain will initially address the need for enhanced training, operational efficiency and knowledge management in the nuclear industry. This partnership strongly validates the value proposition Atlantis brings to the energy sector and is an important step in the Company’s ongoing efforts to diversify its business. For further discussion, refer to “Powertrain” on page 11.

- At the Company's Annual Meeting of Shareholders held June 12, 2008, additional individuals were nominated for election as directors by proxy holders present at the meeting and four new directors were elected, refer to Changes to the Board of Directors on page 11.
- On April 7, 2008 the Company announced that it has been awarded several new contracts valued at approximately Cdn\$3.0 million. Work under these contracts is expected to be completed during 2008. The contracts include the delivery by ASA of an Advanced Electronic Classroom to provide systems and maintenance training for U.S. military aircraft maintenance personnel; a contract from a major partner in the energy sector that will see Atlantis' IMTS used as a prototype for training technicians in power plants; and follow-on orders for a number of technologies and programs.
- Due to the complexity of the purchasing decision making process in the military sector, our status as a subcontractor and the large size of individual contracts relative to our lower revenue base it has become increasingly difficult to forecast future revenues. Accordingly, the Company withdraws its revenue guidance previously provided and does not plan to provide future revenue guidance until further notice.

2. FORWARD-LOOKING STATEMENTS

Forward-looking statements look into the future and provide an opinion about the effect of certain events and trends on the business. Forward-looking statements may include words such as "plans", "intends", "anticipates", "should", "estimates", "expects", "believes", "indicates", "targeting", "suggests" and similar expressions.

This MD&A, and in particular the Business Outlook for 2008 on page 30, contains forward-looking statements. These forward-looking statements are based on current expectations and various estimates, factors and assumptions, and involve known and unknown risks, uncertainties and other factors. The material factors and assumptions that were applied in making the forward-looking statements in this MD&A include assumptions regarding: our ability to win new projects; to successfully complete ongoing negotiations with new and existing customers for new work and to accurately forecast the timing of such wins; our ability to raise new capital on reasonable terms; our ability to meet debt obligations and operate as a going concern; our ability to win new projects; the amount of tax credits available to us under the Ontario Interactive Digital Media Tax Credit; the success of our cost reduction plan and the timing for its achievement; our current order backlog and the timing of its recognition; our ability to protect and exploit our intellectual property; our ability to meet contractual obligations under the CFTS program or any other major program; our ability to complete new and existing projects on time and on budget; the performance of subcontractors generally; the development of applications, market and market share for our HVTT product; the stability and growth of military markets and expenditures worldwide and expected developments in the energy and aerospace industry; the value of the Canadian dollar relative to foreign currencies, in particular, the US dollar; the stability and growth of markets for simulation based training products; and the fair value of our Company exceeding its carrying value in the financial statements including goodwill.

It is important to note that:

- Unless otherwise indicated, forward-looking statements in this MD&A describe our expectations as of August 13, 2008.
- Readers are cautioned not to place undue reliance on these statements as our actual results, performance or achievements may differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements if known or unknown risks, uncertainties or other factors affect our business, or if our estimates or assumptions prove inaccurate. Therefore, we cannot provide any assurance that the predictions of forward-looking statements will materialize.
- We assume no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or for any other reason, except as required by applicable securities laws and regulations.

Material factors that could cause our actual results to differ materially from the forward-looking statements in this MD&A include risks and uncertainties relating to but not limited to: our ability to convert sales, negotiations and marketing pursuits into actual awards and order backlog; our ability to source capital to fund our operations on reasonable terms; our ability to repay debt on demand should it be required due to breach of covenants or other reasons; our ability to operate as a going concern; our ability to qualify under the Ontario Interactive Digital Media Tax Credit; our ability to execute the cost reduction plan; the availability of skilled personnel; our reliance on subcontractors; our ability to protect the ownership of our technology and intellectual property; continued reliance on key customers for existing and new work; our ability to successfully launch and manage the Powertrain joint venture; the level of military expenditures and developments in the energy and aerospace industries; the volatility of foreign exchange rates; the strengths of the Canadian and US economies; our continued ability to integrate our third quarter 2007 acquisition, ASE; and our ability to leverage off the CFTS program.

For additional information regarding risks and uncertainties that could affect our business, please see the Business Risk Factors section of this MD&A and the Description of the Business – Risk Factors section in our Annual Information Form, both of which are available on the System for Electronic Data and Retrieval (“SEDAR”) at www.sedar.com.

Additional information regarding our Company is contained in filings with securities regulatory authorities, including our Annual Information Form and Management Information Circular. These documents are available on SEDAR or on our website at www.atlantissi.com

3. WHO WE ARE

Since our Company was founded 30 years ago, we have developed into a well recognized provider of simulation-based training technology primarily targeted to the military and commercial aviation industries, where we have gained a solid reputation for our technological capabilities and innovative solutions. More recently, we have expanded into the energy industry. In June 2008, we announced a joint venture with the PWUTI to create Powertrain, which is

focused on becoming a “Centre of Excellence” in training for the global energy sector. Powertrain will initially focus on addressing the growing need for enhanced training, operational efficiency and knowledge management in the nuclear industry.

In recent years, the Company has broadened its capabilities and transformed itself from a provider of flight and flight maintenance training products to a provider of integrated training systems and learning solutions. Our current mix of competencies includes: simulation, e-learning and knowledge management systems and expertise, hardware and software integration and virtual reality. We are focused on performance outcomes and on the means for ensuring optimal performance enhancement that can be measured and sustained. Subject matter expertise in both training and learning ensures that we deliver the performance results expected by our customers.

We are headquartered in Brampton, Ontario and maintain offices in Orlando, Florida and Halifax, Nova Scotia. Powertrain is headquartered in Toronto and maintains an advanced nuclear training facility in Tiverton, Ontario

Our Core Values

- Quality – we focus on our customers, their requirements and expectations.
- Innovation – we use responsible creativity to craft the best solutions.
- Integrity – we act ethically in our professional endeavours.
- Accountability – we are responsible and meet our commitments.
- Teamwork- we believe in spirited collaboration.

4. OUR MARKETS

Military

Our roots are in the military and we will continue to strengthen our position in this market.

There are a number of important trends in the military that favour the services we provide:

- there is a trend towards outsourcing to better manage military budgets and to encourage more innovative training solutions;
- expected high levels of attrition across armed forces creates a requirement to train more qualified technicians and trainers in less time;
- the nature of warfare is changing and the use of sophisticated computer systems in communications, weapons delivery and networking lends itself perfectly to the use of synthetic training and performance based learning systems;
- with the advent of more powerful computers, more sophisticated peripheral technology and enhanced graphics, the realism in simulation is unprecedented resulting in an ever-increasing acceptance of this learning approach by the military; and

- the cost of simulation technology has been drastically reduced making it much more affordable to a wider base of applications and users.

The Canadian Forces has an unprecedented number of major acquisition programs either underway or planned including new airlift airframes, modernization of the frigates, new multi-purpose ships, new trucks and tanks, a replacement fixed-wing search and rescue platform and arctic patrol boats, as well as other recently announced programs. All of these programs will require performance critical learning systems. Our capabilities position us well to capture a significant share of the training dollars for these programs.

The US military spends about US \$500 billion per year and accounts for approximately 50% of the global military spending. Our presence in this market is not only important because of the sheer size of the market but also because the US military can dictate or strongly influence who can be a supplier of goods and services for US military sales to foreign governments. To access this market directly it was essential to establish a presence in the US, gain the required security clearances and meet US government procurement policies. ASA was created for this purpose.

Energy

From the early 1970s to the mid 1980s, nuclear energy in the US grew from about 2% to 19% of electrical supply and has remained relatively constant since that time due to heightened societal concerns about nuclear energy. We believe that this fact has several interesting implications for us:

- a significant number of these facilities have reached an age where major retrofits and upgrades are required to serve existing power demand; and
- the societal concerns around nuclear safety and the subsequent reduction in capacity at existing plants, coupled with the lack of new plants being built since the mid 1980s has resulted in both a lack of jobs and the reduction of formal training programs at many colleges and universities as fewer people were entering the nuclear industry.

The increased demand for reduced carbon emissions is prompting a renaissance of nuclear energy as the only viable source in large quantities of emission free energy. This anticipated increase in demand, as well as the demand for retrofits, major upgrades and the impending attrition or retirement of a significant portion of an aging workforce are expected to result in a significant training requirement.

The need to reduce carbon emissions is generating significant interest in emission free generation of electricity. In 2006, nuclear energy and hydro accounted for 73% and 25% respectively of the US sources of emission free generation. Other emission free sources such as solar, wind and geothermal accounted for only 2.6% of the emission free generation. While these other sources will continue to grow, it is our belief that nuclear energy is the only viable cost effective vehicle to deliver substantial emission free power for the foreseeable future.

Globally, the nuclear power industry is entering a significant growth phase, with 30 new reactors under construction and another 300 are being planned or proposed. In Ontario alone, it is estimated that \$26 billion will be spent on the building of new nuclear facilities and the

rehabilitation of existing operations over the next 20 years. This expected growth has created a significant human resources challenge for the industry as a high percentage of skilled operators and other employees are nearing retirement age. In Canada, for example, 38% of the workforce is over the age of 50.

Atlantis secured its first orders for this market in 2006 and 2007 and in the second quarter of 2008 announced an important joint venture with the PWUTI to create Powertrain – a “Centre of Excellence” in training for the global energy sector. Powertrain is initially focusing on addressing the growing need for enhanced training, operational efficiency and knowledge management in the nuclear industry.

Civil Aviation

We have been involved with the civil aviation industry since our inception, and continue to view this market with interest. We expect the coming years will bring an unprecedented worldwide shortage of qualified commercial pilots due to the following trends:

- a significant global growth in civil aviation that is expected to continue;
- a significant proportion of the pilot population is approaching retirement age; and
- fewer military pilots are transferring to civil aviation.

Boeing estimates that 29,000 new airliners are required by 2026, for a staggering market value of US \$2.8 trillion. It estimates that these new planes will require an additional 18,000 new pilots every year for the next 20 years, for a total of 360,000 new pilots.

Our flight training devices, cockpit procedures trainers and flight simulators are installed and operating around the world, and we will continue to take a keen interest in the civil aviation industry worldwide.

Over the last several years, we have invested in developing the HVTT, our virtual-reality, full-motion helicopter simulator. By using virtual reality this product has the potential of providing full flight simulation training at a fraction of the cost of full flight simulators. We have signed a memorandum of understanding with a major North American commercial aviation training company to conduct further field tests at one of its training facilities. These field tests are expected to commence in the third quarter of 2008. The field trials have been delayed due to our difficulty in sourcing adequate production quality virtual reality head gear. This problem is expected to be resolved shortly.

Other

We believe that there are numerous other markets that would benefit from our synthetic learning systems. These include the medical industry, complex industrial facilities and the transportation industry. We do not intend to actively pursue these industries at this time unless an unexpected opportunity arises.

5. OUR VALUE EQUATION

We believe that our integrated training systems and learning solutions allow our customers:

- to train students economically;
- to significantly reduce instructor-to-student ratio;
- to significantly reduce the cost of training by freeing up expensive assets such as fighter planes and full flight simulators through the use of simulation and virtual reality;
- to speed up the learning process and enhance the quality of learning through continuous performance assessment, feedback mechanisms and the realism of the training simulation;
- to maintain training consistency and discipline between groups that trained at different times and by different instructors;
- to pre-screen students for their suitability in the operational roles; and
- to cost effectively update their training programs.

6. OTHER COMPANY INFORMATION

We are registered under a number of quality management programs including ISO 9001:2000, AS9100:2004, CSA-Z299.1-1985, Boeing BQMS D6-82479 and Rockwell Collins RC-9000, among others.

We operate in the United States through our wholly-owned subsidiary ASA. We operate in Canada and the rest of the world through our wholly-owned subsidiary ASI, and the recently acquired ASE division, a division of ASC.

At March 31, 2008, we had a total head count of 159, of which 38 were based at ASA in Orlando, Florida and 23 were with the ASE division in Halifax, Nova Scotia.

7. THE CFTS PROGRAM

Early in the second quarter of 2005, the Allied Wings consortium (we are one of five members led by Kelowna Flightcraft Ltd. as the prime contractor) was awarded a \$1.77 billion contract for the CFTS program by the Canadian Department of National Defence (“DND”) and the Canadian Forces (“CF”) to provide the design, development, installation, operation and support for the CFTS ground-based training system in Southport, Manitoba for a twenty-three year period. Our portion of the contract, which started in 2005, is currently expected to generate approximately \$71.3 million in revenues for the initial phase and a further approximately \$18.3 million for the twenty-year support services phase which will be recognized over the twenty-three years. The initial phase of our contribution to the CFTS program involves the provision of an integrated training solution to the consortium. We, including ASA, are developing and manufacturing

some components of this solution (“in-house” portion), while a significant portion will be provided by other companies (“subcontractor” portion).

Throughout 2007 and the first half of 2008, we continued to deliver on our commitments under the CFTS program. To date, we have recognized revenues of \$16.8 million, \$26.3 million, \$22.6 million and \$3.7 million in 2005, 2006, 2007 and the first half of 2008, respectively, for a total of \$69.4 million, leaving approximately \$20.2 million yet to be recognized on the contract, including the \$17.8 million 20-year support phase; the support phase of the program commenced in the fourth quarter of 2007. The support revenues have been combined with the initial phase revenues for subsequent presentation in this document.

8. COST REDUCTION PLAN

The Company initiated a cost reduction plan in the fourth quarter of 2007. The cost reduction plan is aimed at reducing costs and overall operating expenses by approximately 15% annually. Workforce reductions and other cost cutting measures are expected to result in annualized savings of approximately \$6.4 million. The expected savings from the plan in 2008 are approximately \$4.0 million. This plan resulted in one time termination costs of approximately \$802, which were recorded in the fourth quarter of 2007.

The cost reduction plan is not expected to impact the Company’s ability to execute current contracts or pursue or execute new opportunities that have been identified. Workforce reductions are primarily focused on non-revenue generating positions. While the Company plans to reduce costs at its ASA operations it will continue to maintain a presence in the US and retain the security clearances required to meet US government procurement policies.

9. CHANGES TO BOARD OF DIRECTORS

At the Company’s annual meeting of shareholders, which was held on June 12, 2008, additional individuals were nominated for election as directors by proxy holders present at the meeting. The vote for the election of directors was conducted by way of a ballot. The Board now consists of re-elected directors Andrew Day, David McFadden and David Williams and newly elected directors Mark Rivers, Richard Rosenblum, Ralph Wegner and Lyell Farquharson.

10. POWERTRAIN

We reached an important milestone in our energy market strategy with the announcement, in June 2008, of a joint venture with the Power Workers Union Training Institute (PWUTI), a wholly owned subsidiary of the Power Workers’ Union. Under this joint venture, we created a new company called Powertrain, which is focused on becoming a “Centre of Excellence” in training for the global energy sector. Powertrain is headquartered in Toronto and will maintain an advanced nuclear training facility in Tiverton, Ontario.

Powertrain will initially focus on addressing the need for enhanced training, operational efficiency and knowledge management in the nuclear industry. Powertrain is currently developing a unique, fully integrated, systematic approach to training that will employ simulations, e-learning and knowledge management applications for capturing industry-critical

knowledge and know-how from experts in the field, feeding this back to the students in physical and virtual classrooms to significantly enhance the relevancy of the training experience.

We believe that PWUTI's intimate knowledge of the industry and established relationships, coupled with our expertise in simulation, virtual reality and e-learning, will facilitate Powertrain's acceptance and its penetration in the large and growing energy market.

Powertrain is equally owned and jointly operated by Atlantis Systems Corp. and PWUTI. Atlantis will be contributing intellectual property related to maintenance training, e-learning and knowledge management. PWUTI will be contributing an investment of approximately \$1.6 million in three tranches of \$533,333 within the next two years. Under the terms of the Shareholders Agreement, Powertrain will provide a scientifically based, technologically advanced, and an academically supported solution to the Energy Industry's training needs in the face of the looming workforce "Greyout". Powertrain will augment Atlantis' training systems with industry experts, consulting services and subject matter expertise in the areas of training, learning and knowledge management. Powertrain is currently engaged in conducting feasibility studies for seven distinct training related projects in the energy sector.

11. MISSED REGULATORY FILING DEADLINE

On March 25, 2008, subsequent to the 2007 year end, the Company issued a press release announcing that it would not be able to meet the regulatory filing deadline of March 31, 2008, for filing with the securities regulatory authorities in Ontario and Quebec, its annual financial statements, management discussion and analysis and annual information form for the fiscal year ended December 31, 2007 and the related certifications (the "Annual Filings"). The reason for the delay in the filing of the Annual Filings was that the Company was seeking to refinance its bank credit facility with a new lender. If the new lender did not proceed with the financing and the bank demanded repayment of its term loan, the Company would need to assess its financial position as at December 31, 2007 on the basis that it would not be able to meet the "going concern" test for the following twelve month period. The Company filed an application with the Ontario Securities Commission requesting that it be subject to a "management" cease trade order, prohibiting its directors, officers and other insiders from trading the Company's securities until the Annual Filings have been filed, rather than an "issuer" cease trade order. A follow-on press release was issued on April 1, 2008 confirming the delay in the release of the Annual Filings and that the Ontario Securities Commission was expected to issue a temporary "management" cease trade order, rather than issuing an "issuer" cease trade order. On April 1, 2008 the temporary "management" cease trade order was issued and the affected persons were notified. On May 7, 2008 the Company completed its Annual Filings and on May 12, 2008 the "management" cease trade order was lifted.

12. OVERVIEW

Selected Quarterly Information

	Quarter Ended	Quarter Ended
	June 30, 2008	June 30, 2007
	\$	\$
Revenues	4,245	15,241
Gross margin	414	5,505
Gross margin percentage	9.8%	36.1%
Operating expenses ⁽¹⁾	1,920	2,730
Depreciation and amortization	522	171
Interest expense and financing costs (income), net	309	(67)
Net (loss) income per share (basic)	(2,337)	2,671
Net (loss) income per share (basic)	(0.04)	0.05
Total assets	23,799	28,587

⁽¹⁾ Includes selling and marketing (“S&M”), general and administrative (“G&A”) and stock option expense

Revenues for the second quarter of 2008 decreased by 72.1% to \$4,245 from \$15,241 for the same period in 2007, primarily due to reduced revenues from the CFTS program and lack of new order flow to replace the reduced CFTS revenues. Revenues from the CFTS program decreased in the second quarter of 2008 by \$10,595 to \$1,888 of the same period last year. The CFTS contract represented 44% of revenues in the second quarter of 2008 versus 82% of revenues for the same period in 2007.

Gross margin for the second quarter of 2008 was \$414, or 9.8% of revenue, versus \$5,505, or 36.1% of revenue, for the corresponding period in 2007. The gross margin for the second quarter of 2008 included a reduction of \$163 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program. The lower gross margin percentage in the second quarter of 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are independent of projects and not directly variable. We expect our gross margin percentage to increase in the remainder of 2008 but will continue to fluctuate depending on the mix of CFTS to non CFTS revenue.

Operating expenses (defined as combined General and Administrative (“G&A”), Selling and Marketing (“S&M”) and stock option expenses) decreased in the second quarter of 2008 by 30% to \$1,920, primarily due to the net effect of the continuation of our cost reduction plan. For the second quarter of 2008, we incurred depreciation and amortization expense of \$522, versus \$171 for the same period in the prior year. This increase of \$351 primarily reflects the commencement of amortization of the HVTT in the third quarter of 2007 and the amortization of the core technology acquired in the Eduplus transaction, offset, in part, by a decrease in the level of investment in capital assets to \$16 in the second quarter of 2008 from \$192 for the same period in 2007.

Interest and financing costs resulted in a net expense of \$309 for the quarter ended June 30, 2008 versus a net income of \$67 for the same period in the prior year. Net interest expense for the

second quarter of 2008 of \$309 represents interest and accretion expense of \$193 and finance and bank charges, support fees and other costs of \$128, offset, in part, by interest income of \$12. Interest and financing net income of \$67 for the quarter ended June 30, 2007 represents interest income of \$71, offset in part, by interest expense of \$3 and finance and bank charges, service charges and other costs of \$1.

Net loss for the second quarter of 2008 of \$2,337 compared to a net income \$2671 for the second quarter of 2007. In the second quarter of 2008, ASA accounted for \$209 of the loss compared to \$404 in the second quarter of 2007. The decrease in ASA's loss is primarily due to higher gross margins on the contracts started in the first quarter of this year.

Total assets of \$23,799 at June 30, 2008 represented a decrease of \$4,788 or 17% from June 30, 2007. The decrease is primarily due to a decrease in cash and trade and other receivables.

13. RESULTS OF OPERATIONS

The following is a discussion of the material factors influencing the operating results and the financial condition of our Company, as at, and for three months ended June 30, 2008 with comparisons to the three months ended June 30, 2007, where applicable.

The Consolidated Statements of Operations, Comprehensive Loss and Deficit for the three months ended June 30, 2008, with comparative numbers for the same period in 2007 reflect the operations of our operating entities, ASI, ASA and ASE (a division of ASC) and corporate overheads.

14. REVENUE

Second Quarter

The components of revenue for the three months ended June 30, 2008 and 2007 are as follows:

	Three months ended June 30			
	2008		2007	
	\$	%	\$	%
CFTS	1,888	44%	12,483	82%
RDAF	304	7%	1,242	8%
IMTS	77	2%	992	7%
SMHP	638	15%	-	0%
Energy Sector	433	10%	53	0%
Other	905	22%	471	3%
Total	4,245	100%	15,241	100%

We realized consolidated revenues of \$4,245 in the second quarter of 2008, a decrease of \$10,996, or 72.1% from the same period in 2007. The decrease in revenues in the second quarter of 2008 over that of 2007 was the result of reduced revenues from the CFTS program of \$10,595, RDAF of \$938 and IMTS of \$915, offset, in part, by revenues from SMHP of \$638 as

well as increased revenues from the energy sector of \$380 and other of \$434.

We began to recognize revenues from the CFTS program in the second quarter of 2005 under the terms of an initial enabling contract with Kelowna Flightcraft, the CFTS prime contractor. For the CFTS program, we recognize revenue based upon the work performed in-house (including the delivery of courseware created by ASA, acting as a subcontractor to ASI under the CFTS program), materials used and achievement of milestones by our subcontractors on the program. As a result, the revenue recognized from this program has fluctuated.

Through to the end of the second quarter of 2008 we have recognized, in total, \$69.4 million of revenue out of a total contract value of \$89.6 million from the CFTS program. We expect ASA and ASI to continue to develop and deliver courseware for the CFTS program throughout most of 2008. CFTS program revenue for the initial production portion of the project is entering into the mature phase where production is diminishing, as expected, as it moves closer to completion.

The CFTS contract value also includes approximately \$18.3 million in support services that will be substantially recognized over a twenty year period following the initial phase of the program. The service program started in the fourth quarter of 2007.

When appropriate, we deliver services to foreign customers or prime contractors through Canadian Commercial Corporation, which may act as a contractual intermediary and guarantees contract completion. However, the following discussion of our revenues identifies the end customers who ultimately received the products and services.

In the third quarter of 2006, we were awarded a contract to provide a Cockpit Procedures Trainer (“CPT”) to the RDAF for the EH-101 helicopter through prime contractor AgustaWestland. The program is expected to be completed in 2008. Revenues of \$1,156, \$5,072 and \$2,229 were recognized for this program in 2008 to-date, 2007 and 2006, respectively.

In the second quarter of 2008, revenues from IMTS projects decreased to 2% of total revenues, or \$77, as compared to 7%, or \$992, for the same period in 2007. This decrease of \$915 from the second quarter of 2007 is primarily due to the completion of the initial phase of a contract to provide weapons load trainers to the Canadian Forces (“CF”) in 2008. The second quarter of 2007 IMTS revenue is primarily due to contracts with the CF. In the second quarter of 2006, the CF awarded us with a contract to provide weapons load trainers (which expanded our IMTS offering) for the CF-18 aircraft fleet, along with support services through 2020.

With the Eduplus acquisition in the third quarter of 2007 we acquired the SMHP contract. The Eduplus division will provide the SMHP with training design, training documentation and courseware production. We recognized \$638 in revenue for the second quarter of 2008 (2007 – nil) from this project. Backlog at June 30, 2008 was \$7.7 million and we expect revenues from this project through 2011.

Revenues from customers in the energy sector increased in the second quarter of 2008 to \$433, a 717% increase from the same period in the prior year. Our pursuit of the training business associated with nuclear technicians and operators is a relatively new sector for our

Canadian operations. Our strategic market initiative commenced in late 2005 and we signed our first contract in this sector in the first quarter of 2006. Three additional contracts were signed for hardware and software engineering services through the rest of 2006 and three of these projects were renewed in 2007 and remain active as of June 30, 2008. In the first quarter of 2008, we signed a contract with a major partner in the energy sector that will see Atlantis' IMTS used as a prototype for training technicians in power plants.

Other revenues in the second quarter of 2008 of \$905 includes \$410 from one contract awarded to ASA from a US defense contractor in the second quarter of 2007 as well as two additional contracts awarded by the same contractor in the first quarter of 2008 and \$495 derived from a number of small, short-duration contracts. Other revenues in the second quarter of 2007 for \$471 included revenue of \$138 from the upgrade of our existing Atlantis-Boeing 767 flight training devices for Air Canada, along with \$333 derived from a number of small, short-duration contracts.

During the second quarter of 2008 we had contracts with multiple customers, however, one customer, the CF, represented 45% of revenue (88% in the same period of 2007). In addition, as at June 30, 2008, the same customer represented 35% of combined accounts receivable and unbilled revenue (30% in the same period of 2007). Our second largest customer, Sikorsky, represented 15% of revenue (0% in the same period of 2007) and 16% of the combined outstanding balance of accounts receivable and unbilled revenue (0% in the same period of 2007) at quarter end.

The order backlog at June 30, 2008 was \$32.1 million, which consisted of \$20.2 million from the CFTS program (including approximately \$17.8 million in CFTS support services), \$7.7 million from the SMHP, \$2.5 million from ASA's contracts with a US defense contractor, \$0.7 million from the CPT program for the RDAF, and \$1 million from all other contracts. The order backlog of \$32.1 at June 30, 2008 has decreased \$6.8 million from the comparable backlog of \$38.9 million (which included \$18.4 million in CFTS support services for the twenty-year support period) at June 30, 2007. This order backlog decrease consisted of a \$10.1 million net reduction in the CFTS program, offset, in part by a \$3.3 million net increase in the non-CFTS order backlog. The \$3.3 million net increase in the non-CFTS program backlog was due, primarily, to the addition of \$7.7 million backlog for the newly acquired SMHP contract, offset, in part, by the recognition of revenue on non-CFTS projects.

We expect between 25% and 30% of the order backlog to be realized as revenue in 2008. We anticipate lower consolidated revenues in 2008 than experienced in 2007 due to anticipated new programs coming in late in the year.

Order backlog is defined as that portion of a legally binding commercial agreement that provides sufficient detail on our obligations and our customers' obligations to form the basis for a contract and an order that has not yet been recognized as revenue.

Six months

The components of revenue for the six months ended June 30, 2008 and 2007 are as follows:

	Six months ended June 30			
	2008		2007	
	\$	%	\$	%
CFTS	3,677	43%	15,342	73%
RDAF	1,156	13%	2,687	13%
IMTS	201	2%	1,550	7%
SMHP	1,187	14%	-	0%
Energy Sector	500	6%	182	1%
Other	1,863	22%	1,309	6%
Total	8,584	100%	21,070	100%

Revenue for the six months ended June 30, 2008 was \$8,584, a decrease of \$12,486, or 59.3% from the same period in 2007. Revenue for the CFTS program was \$3,677 for the six months ended June 30, 2008, compared to \$15,342 for the comparable period in 2007, an \$11,665 decrease. CFTS program revenue for the period reflect the entering of the production portion of the project into the mature phase where production is diminishing, as expected, while production moves closer to completion. RDAF revenues were \$1,156 for the period in 2008, a reduction of \$1,531 versus the \$2,687 for the corresponding period in 2007. IMTS revenues were \$201 for the period in 2008, a reduction of \$1,349 versus the \$1,550 for the corresponding period in 2007.

The overall revenue decrease of \$12,486 for the six months year-over-year represents a decrease of \$11,665 for the CFTS program, a decrease of \$1,531 for the RDAF helicopter cockpit procedures trainer, a decrease of \$1,349 for IMTS, offset by an increase of \$1,187 for SMHP, an increase of \$318 for the energy sector and a \$554 increase from other short-duration contracts (included in Other revenue).

During the six months ended June 30, 2008, while we had contracts with multiple customers, one customer, the CF represented 43% of revenue. Our second-largest customer represented 14% of revenue.

During the six months ended June 30, 2007, one customer, the CF represented 79%. Our second-largest customer represented 13% of revenue for the same period in 2007.

15. GROSS MARGIN

Second Quarter

Gross margin for the second quarter of 2008 was \$414, or 9.8% of revenue, versus \$5,505, or 36.1% of revenue, for the corresponding period in 2007. The gross margin for the second quarter of 2008 included a reduction of \$163 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program. The lower gross margin percentage in the second quarter of 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are

independent of projects and not directly variable. Gross margins will continue to fluctuate depending on the mix in a particular quarter between lower-margin CFTS revenue and non-CFTS revenue.

Six months

Gross margin for the six months ended June 30, 2008 was \$561, or 6.5% of revenue, versus \$6,731, or 31.9% of revenue, for the corresponding period in 2007. The gross margin for the six months ended June 30, 2008 included a reduction of \$512 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program.

16. OPERATING EXPENSES

Second Quarter

We incurred G&A expenses of \$1,416 for the three months ended June 30, 2008, a 27% decrease over the same period in 2007. The G&A expense for the second quarter of 2008 reflects a reduction of \$104 in costs incurred by ASA in the same period of 2007, which is primarily the result of implementation of our cost reduction plan. The remaining decrease of \$415 at the Canadian operations is due primarily to the decrease of administration personnel and related expense over the second quarter levels of the prior year as a result of implementation of our cost reduction plan, offset in part, by \$68 of expense incurred by the new division, ASE.

S&M expense was \$468 for the three months ended June 30, 2008, a 36% decrease as compared to the same period in 2007. The second quarter of 2008 reflects a reduction of \$73 from the S&M expense incurred by ASA in the same period of 2007. This reduction in S&M spending at ASA is primarily the result of implementation of our cost reduction plan. The remaining decrease of \$194 at the Canadian operations is due primarily to the decrease of marketing personnel and programs over the first quarter levels of the prior year due to the implementation of the our cost reduction plan, offset in part, by \$68 of expense incurred by the new division, ASE.

We recorded stock option expenses of \$36 for the three months ended June 30, 2008 versus \$60 for the same period in 2007.

In summary, operating expenses (which represent the sum of G&A, S&M and stock option expenses) were \$1,920 for the second quarter of 2008 versus \$2,730 for the same period last year, a decrease of \$810 or 30%. Of this decrease, \$177 and \$609 was due to decreases in operating expenses incurred by ASA and Canadian operations respectively in the second quarter of 2008. The decreases were primarily the result of implementation of the cost reduction plan.

Six months

We incurred G&A expenses of \$2,854 for the six months ended June 30, 2008, a 27% decrease over the same period in 2007. The G&A expense for the six months ended June 30, 2008

reflects a reduction of \$248 in costs incurred by ASA in the same period of 2007, which is primarily the result of implementation of our cost reduction plan. The remaining decrease of \$830 at the Canadian operations is due primarily to the decrease of administration personnel and related expense over the second quarter levels of the prior year as a result of implementation of our cost reduction plan, offset in part, by \$140 of expense incurred by the new division, ASE.

S&M expense was \$835 for the six months ended June 30, 2008, a 49% decrease as compared to the same period in 2007. The S&M expense for the six months ended June 30, 2008 reflects a reduction of \$229 from the S&M expense incurred by ASA in the same period of 2007. This reduction in S&M spending at ASA is primarily the result of implementation of our cost reduction plan. The remaining decrease of \$583 at the Canadian operations is due primarily to the decrease of marketing personnel and programs over the first quarter levels of the prior year due to the implementation of the our cost reduction plan, offset in part, by \$131 of expense incurred by the new division, ASE.

We recorded stock option expenses of \$72 for the six months ended June 30, 2008 versus \$102 for the same period in 2007.

In summary, operating expenses (which represent the sum of G&A, S&M and stock option expenses) were \$3,761 for the six months ended June 30, 2008 versus \$5,681 for the same period last year, a decrease of \$1920 or 34%. Of this decrease, \$477 and \$1,413 was due to decreases in operating expenses incurred by ASA and Canadian operations respectively in the second quarter of 2008. The decreases were primarily the result of implementation of the cost reduction plan.

17. OTHER ITEMS

Second Quarter

We incurred depreciation and amortization expense of \$522 in the three months ended June 30, 2008 versus \$171 in the same period of 2007. This increase of \$351 primarily reflects the commencement of amortization of the HVTT in the third quarter of 2007 of \$105 and the amortization of the core technology acquired in the Eduplus transaction of \$265.

Interest and financing costs resulted in a net expense of \$309 in the three months ended June 30, 2008 as compared to income of \$67 in the same period of 2007. The second quarter 2008 net expense of \$309 represents interest expense of \$193 and finance and bank charges, support fees and other costs of \$128, offset, in part, by interest income of \$12. The 2007 second quarter net income of \$67 includes \$71 for interest income, offset in part by, interest expense of \$3, and finance and bank charges, support fees and other costs of \$1.

Six months

We incurred depreciation and amortization expense of \$1,052 in the six months ended June 30, 2008 versus \$324 in the same period of 2007. This increase of \$728 primarily reflects the commencement of amortization of the HVTT in the third quarter of 2007 of \$209 and the amortization of the core technology acquired in the Eduplus transaction of \$531.

Interest and financing costs resulted in a net expense of \$387 in the six months ended June 30, 2008 as compared to income of \$169 in the same period of 2007. The six months ended June 30, 2008 net expense of \$387 represents interest expense of \$241 and finance and bank charges, support fees and other costs of \$179, offset, in part, by interest income of \$33. The six months ended June 30, 2007 net income of \$169 includes \$180 for interest income, offset in part by, interest expense of \$5, and finance and bank charges, support fees and other costs of \$6.

18. OTHER EXPENSES

There was no income tax (recovery) expense shown for the three months ended June 30, 2008 or the same period in 2007 because we had previously recorded a full valuation allowance for all future income tax assets (specifically cumulative operating loss carry-forwards and temporary differences) as we believed there was uncertainty in realizing the full benefit of these items. As a result, any income tax recovery or expense related to losses and earnings in the second quarter of 2008 and in the same period in 2007 were offset by utilizing an equal portion of the unrecognized operating loss carry-forwards from previous years. As at June 30, 2008, we continue to carry a full valuation allowance against our income tax assets due to the continued uncertainty surrounding their full usage. There will be no income tax expenses against earnings in Canada until either all unrecognized operating loss carry-forwards of approximately \$12,311 are used or expire. \$1,767 of the carry-forwards expire in 2008 and the balance expire between 2009 and 2027. Furthermore, there will be no income tax expense against earnings in the United States until all unrecognized operating loss carry forwards of approximately \$4,183 are used or expire. The carry-forwards expire between 2026 and 2027.

19. NET INCOME

Second Quarter

For the three months ended June 30, 2008, we recognized a loss of \$2,337, or \$(0.04) per share, compared to earnings of \$2,671, or \$0.05 per share, for the same period in 2007. The calculation of diluted net income (loss) per share for the first quarters of 2008 and 2007 did not result in any dilution versus reported basic earnings per share.

The loss for the second quarter of 2008 included the following items of note:

- The gross margin for the second quarter of 2008 included a reduction of \$163 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program. The lower gross margin percentage in the second quarter of 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are independent of projects and not directly variable.
- Combined operating expenses (including depreciation and bank service charges) of \$408 for the ASE division, subsequent to the Eduplus acquisition in the third quarter of 2007. In addition, we recognized revenue in ASE, primarily from the SMHP, of \$683; and

- \$810 reduction in operating expenses (which represent the sum of G&A, S&M and stock option expenses) from the same period in 2007, primarily, as a result of implementation of the cost reduction plan.

Six months

For the six months ended June 30, 2008, we recognized a loss of \$4,639, or \$(0.08) per share, compared to earnings of \$896, or \$0.02 per share, for the same period in 2007. The calculation of diluted net income (loss) per share for the first six months of 2008 and 2007 did not result in any dilution versus reported basic earnings per share.

The loss for the six months ended June 30, 2008 included the following items of note:

- The gross margin for the six months ended June 30, 2008 included a reduction of \$512 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program. The lower gross margin percentage in the six months ended June 30, 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are independent of projects and not directly variable.
- Combined operating expenses (including depreciation and bank service charges) of \$815 for the ASE division, subsequent to the Eduplus acquisition in the third quarter of 2007. In addition, we recognized revenue in ASE, primarily from the SMHP, of \$1,251; and

\$1,920 reduction in operating expenses (which represent the sum of G&A, S&M and stock option expenses) from the same period in 2007, primarily, as a result of implementation of the cost reduction plan.

20. SUMMARY OF QUARTERLY RESULTS (UNAUDITED)

Following are the quarterly results for 2008, 2007 and 2006. The table includes the restated amounts only for the first three quarters of 2006.

	2008		2007	
	30-Jun	31-Mar	31-Dec	30-Sep
Revenue	\$ 4,245	\$ 4,339	\$ 5,359	\$ 6,750
Gross margin	414	147	(314)	1,081
Operating expenses*	1,920	1,841	2,483	2,425
Net (loss) income	(2,337)	(2,302)	(3,334)	(1,594)
Net (loss) income per share (basic)	\$ (0.04)	\$ (0.04)	\$ (0.06)	\$ (0.03)

	2007		2006	
	30-Jun	31-Mar	31-Dec	Sep 30 Restated
Revenue	\$ 15,241	\$ 5,829	\$ 11,152	\$ 11,509
Gross margin	5,505	1,226	2,964	3,794
Operating expenses*	2,730	2,951	3,056	2,649
Net (loss) income	2,671	(1,775)	(148)	1,373
Net (loss) income per share (basic)	\$ 0.05	\$ (0.03)	\$ (0.00)	\$ 0.03

*Represents the sum of G&A, S&M and stock option expenses

As previously mentioned, during the first quarter of 2007 we reviewed our revenue recognition for contracts with multiple deliverables and determined that the recognition of revenue for the fourth quarter of 2005 and the first three quarters of 2006 was incorrect. The table above reflects only the restated amounts for each of those two consecutive quarters.

Revenues over the eight-quarter period fluctuated, reflecting our experience with large, multi-year contracts. Our quarterly revenue profile for 2006 reflected fluctuations in CFTS revenue which depended upon the proportion of work performed in-house and the achievement of milestones by our subcontractors in any given quarter. CFTS revenues for each of the last two quarters of 2006 were \$8,202 and \$8,707, respectively. CFTS revenues for each of the quarters of 2007 were \$2,858, \$12,483 and \$4,341 and \$3,010, respectively for a total of \$22,692. CFTS Revenues for the first two quarters of 2008 were \$1,789 and \$1,888 respectively.

Gross margin over the eight quarter period reflects not only revenue changes in each quarter but also certain specific items. The lower gross margin percentage in the fourth quarter of 2006 included a reduction of approximately \$400 due to the recognition of additional costs related to our existing contracts. The lower gross margin percentage in the first quarter of 2007 included approximately \$400 of additional costs relating to research and development, foreign exchange and ASA overhead costs attributed to CFTS courseware development activities. The higher gross margin percentage in the second quarter of 2007 included approximately \$1.8 million of additional revenue as a result of the downward revision in total cost estimates for the CFTS program. The lower margin percentage in the third and fourth quarters of 2007 is due to lower revenues, higher indirect overheads, and a higher proportion of revenues attributable to the lower margin CFTS program. The lower gross margin in the fourth quarter of 2007 is also the result of a decrease in revenue of \$750 as a result of recalibration of the total cost estimates for the CFTS program. The gross margin for the first quarter of 2008 included a reduction of \$349 as a result

of reconfigured cost estimates to complete the CFTS program. The lower gross margin percentage in the first quarter of 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are independent of projects and not directly variable. The gross margin for the second quarter of 2008 included a reduction of \$163 as a result of reconfigured cost estimates to complete the CFTS program and a reduction of \$168 as a result of reconfigured cost estimates to complete the RDAF program. The lower gross margin percentage in the second quarter of 2008 is also impacted by the inclusion on a lower revenue base of several indirect overheads that are independent of projects and not directly variable.

The net income (loss) for the eight quarters primarily reflects fluctuations in revenue. However, results for the third quarter of 2006 include the effects of the requirement to report the \$3,100 Debentures as a current liability (\$1,064 expense) and the gain on the subsequent repayment of the \$3,000 Debenture (\$224 income), respectively. In addition, the second quarter of 2007 includes the positive effect of the recalibration of total cost estimates on the CFTS program of approximately \$1.8 million in income. The fourth quarter of 2007 reflects the employee severance costs as discussed earlier in the cost reduction plan of approximately \$802 and the decrease in revenue of \$750 as a result of recalibration of the total cost estimates for the CFTS program. The first quarter of 2008 includes a \$1,110 reduction in operating expenses (which represent the sum of G&A, S&M and stock option expenses) from the same period in 2007, primarily, as a result of implementation of the cost reduction plan. The second quarter of 2008 includes a \$810 reduction in operating expenses (which represent the sum of G&A, S&M and stock option expenses) from the same period in 2007, primarily, as a result of implementation of the cost reduction plan.

Net income (loss) per share (basic) also reflected the fluctuations in earnings over the eight quarters as well as the effect of the increase of 3,016,453 in the number of common shares outstanding from December 31, 2006 to December 31, 2007. As at June 30, 2008, the number of outstanding common shares was 55,993,929.

The diluted net income (loss) per share for the eight quarters is not shown since the calculation, using the treasury method, did not result in any dilution versus reported basic earnings per share except for the third quarter of 2006, where diluted earnings per share was \$0.02 versus basic earnings per share of \$0.03. The calculation also resulted in dilution in the second quarter of 2007 however the diluted earnings per share was equal to the basic earnings per share.

CASH FLOW, LIQUIDITY AND CAPITAL RESOURCES

21. CASH FLOW

We had bank indebtedness of \$(1,116) at June 30, 2008 as compared to cash and cash equivalents \$3,652 at June 30, 2007. The sources for the changes in cash and cash equivalents for the three months and six months ended June 30, 2008 and 2007 are as follows:

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2008	2007	2008	2007
Cash flows provided by (used in)				
Operating activities	\$ (775)	\$ (5,274)	\$ (4,397)	\$ (10,611)
Investing activities	(16)	(192)	(36)	(354)
Financing activities	(263)	-	(403)	981
Increase (decrease) in cash and cash equivalents	(1,054)	(5,466)	(4,836)	(9,984)
(Bank indebtedness) cash and cash equivalents at beginning of period	(62)	9,118	3,720	13,636
(Bank indebtedness) cash and cash equivalents at end of period	\$ (1,116)	\$ 3,652	\$ (1,116)	\$ 3,652

22. OPERATING ACTIVITIES

Second Quarter

Cash outflow from operating activities of \$(775) in three months ended June 30, 2008 represented a \$4,499 increase in cash inflow over the comparable quarter of 2007. For the three months ended June 30, 2008, the cash outflows from operating activities of \$(775) were substantially due to a net loss of \$2,337, which resulted in a outflow of \$1,709 after excluding non-cash charges included in the results and by an inflow of 13 from other long-term assets, partially offset by an inflow of \$925 from the net change in non-cash working capital. Non-cash charges to the operating results include depreciation and amortization, stock option expenses as well as accretion on term debt. The \$925 cash inflow on account of net changes in non-cash working capital was primarily due to a decrease in trade and other receivables, partially offset by a decrease in accounts payable and accrued liabilities as well as a reduction in deferred revenue due to recognition of revenue on projects.

Cash outflow from operating activities of \$5,274 in the three months ended June 30, 2007 represented a \$6,563 decrease over cash flow in the comparable quarter of 2006. For the three months ended June 30, 2007, the cash outflows from operating activities of \$5,274 were primarily due to net income of \$2,671 which was increased by non-cash charges included in the results for depreciation and amortization and stock options expenses for a total of \$231. This inflow was more than offset by the net change in non-cash working capital which used \$8,032 of additional cash in the quarter. The \$8,032 cash outflow on account of net changes in non-cash working capital was primarily due to: a reduction in deferred revenue as a result of achievement of CFTS-related subcontractor milestones; an increase in unbilled revenue attributable to the contract with AgustaWestland to provide cockpit procedures trainers to the RDAF; a reduction in accounts payable, partially offset by a reduction in accounts receivable.

Six months

Cash outflow from operating activities of \$(4,397) in six months ended June 30, 2008 represented a \$6,214 increase in cash inflow over the comparable quarter of 2007. For the six months ended June 30, 2008, the cash outflows from operating activities of \$(4,397) were

substantially due to a net loss of \$4,639, which resulted in a outflow of \$3,445 after excluding non-cash charges included in the results, an inflow of 11 from other long-term assets and an outflow of \$955 from the net change in non-cash working capital. Non-cash charges to the operating results include depreciation and amortization, stock option expenses as well as accretion on term debt. The \$955 cash outflow on account of net changes in non-cash working capital was primarily due to a decrease in accounts payable and accrued liabilities.

For the six months ended June 30, 2007, cash outflow from operating activities was \$10,611 representing a \$17,691 decrease over cash inflow in the comparable period of 2006. For the six months ended June 30, 2007, the cash outflows from operating activities of \$10,611 were primarily due to net income of \$896 which was increased by non-cash charges included in the results for depreciation and amortization and stock options expenses for a total of \$425. This inflow was more than offset by the net change in non-cash working capital which used \$11,787 of additional cash in the quarter. The \$11,787 cash outflow on account of net changes in non-cash working capital was primarily due to: a reduction in deferred revenue as a result of achievement of CFTS-related subcontractor milestones; an increase in unbilled revenue attributable to the contract with AgustaWestland to provide cockpit procedures trainers to the RDAF; a reduction in accounts payable, partially offset by a reduction in accounts receivable.

23. INVESTING ACTIVITIES

Second Quarter

For the three months ended June 30, 2008, cash used in investing activities was \$16, as compared to \$192 used for comparable period in 2007.

The 2008 amount represented a \$16 investment in leasehold improvements at ASA due to the move to smaller premises.

Cash used in investing activities was \$192 for the three months ended June 30, 2007 versus \$350 for the comparable period in 2006. The 2007 amount represented investment in capital assets as follows: \$79 represented investment in computer hardware, software, leasehold improvements and furniture and fixtures in ASA and the balance of \$113 primarily represented purchases of computer hardware, software and leasehold improvements in our Brampton, Ontario operating facility.

Six months

For the six months ended June 30, 2008, cash used in investing activities was \$36, as compared to \$354 used for comparable period in 2007.

The 2008 amount represented investment in capital assets as follows: \$17 represented investment in computer hardware, software, leasehold improvements as well as furniture and fixtures in ASA, \$4 represented investment in computer hardware, software, leasehold improvements as well as furniture and fixtures in ASE and the balance of \$15 represented

purchases of computer hardware, communications equipment and leasehold improvements in our Brampton, Ontario facility.

For the six months ended June 30, 2007, cash used in investing activities was \$354 versus \$729 for the comparable period in 2006. The 2007 amount represented investment in capital assets as follows: \$130 represented investment in computer hardware, software, leasehold improvements and furniture and fixtures in ASA and the balance of \$224 primarily represented purchases of computer hardware, software, communications equipment and leasehold improvements in our Brampton, Ontario operating facility.

24. FINANCING ACTIVITIES

Second Quarter

Cash outflow from financing activities for the three months ended June 30, 2008 amounted to \$263, compared to no cash inflow for the same period in 2007.

The cash outflow of \$263 for the three months ended June 30, 2008 represents principal payments on the Term debt and the repayment of the bank term loan from the proceeds of the Comvest Capital LLC term loan.

Six months

Cash outflow from financing activities for the six months ended June 30, 2008 amounted to \$403, compared to a cash inflow of \$981 for the same period in 2007.

The cash outflow of \$403 for the six months ended June 30, 2008 represents principal payments on the Term debt.

The \$981 inflow in the six months ended June 30, 2007 represented proceeds from the exercise of common share purchase warrants of \$873 and the exercise of stock options of \$108.

25. LIQUIDITY

No additional funds were raised through the issuance of debt or equity in 2007 or in the first quarter of 2008, other than proceeds from the exercise of stock options and common share purchase warrants, however, an agreement was signed in the second quarter of 2008 with Comvest Capital LLC.

Effective April 30, 2008, we entered into financing arrangements with ComVest Capital, LLC that provided up to US\$6.6 million of financing in the form of a secured term loan in the amount of US\$2.6 million at a rate of interest of 12.5% per annum payable monthly and 5% per annum of deferred interest, accrued monthly, payable at maturity as well as a secured revolving line of credit of up to US\$4.0 million based on a borrowing base at a rate of interest of US prime plus 2% per annum with a floor of 8%. The term loan matures on April 30, 2011 and the Line of Credit will be available until April 30, 2010, subject to a one-year extension at the option of the Company. These financing arrangements closed May 5, 2008 and the term loan was used to

repay the bank term loan. The arrangement also involved the Company issuing warrants, expiring April 30, 2013, to acquire an aggregate of 9,300,000 common shares at an exercise price of \$0.09 per share. As at June 30, 2008, the Company was out of covenant on its rolling 6-month EBITDA covenant. ComVest agreed to waive the covenant for this period. The Company expects to have further discussions with ComVest on future covenant requirements. These discussions have not been finalized and it is likely that the covenant will be breached at the next compliance date. As a result the term debt has been reclassified as short term debt on the balance sheet.

During the third quarter of 2007, the remaining \$100 Debenture was repaid.

We received \$108 through the exercise of stock options in the three months ended March 31, 2007. In February and March, 2007, 1,456,121 common share purchase warrants were exercised, to purchase common shares at \$0.60 per share. We received proceeds of \$873 as a result of these exercises.

We maintain a committed secured operating line of credit of up to \$4.0 million, based on available borrowing base, with a major US financial firm. US\$2 million of the operating line was utilized as of June 30, 2008. This credit facility permits us to borrow funds directly for operating and subsidiary funding purposes. The facility has financial covenants covering maximum borrowing base based on the prior month accounts receivable balance, minimum earnings before interest, tax, depreciation and amortization (EBITDA) and an annual maximum capital expenditure limit. Any advances are repayable on demand.

At June 30, 2008, the Company was not in compliance with one financial covenant included in the Term Loan and operating line agreement. The covenant in breach was the minimum EBITDA requirement. Our EBITDA year to-date balance of \$(3,200) showed a deficiency of \$(1,200) from the minimum covenant requirement of \$(2,000) however a waiver has been provided. It is likely that the Company will violate covenant requirements at future compliance dates; therefore the entire balance of term debt has been classified as a current liability.

26. CAPITAL RESOURCES

Second Quarter

Stock Options

During the three months ended June 30, 2008, the Company awarded 1,298,986 options to purchase shares of the company under the stock options incentive plan. These options carry a term of 4 years, exercise price of \$0.11 and a vesting period of 1.5 years. The fair value of each option is calculated on the date of the grant using the Black-Scholes option pricing model.

As at June 30, 2008, based on the actual number of common shares outstanding, the Plan would allow for the issuance of a total of 8,399,089 options to purchase common shares of our Company. There are currently 7,267,523 options to purchase common shares outstanding, leaving 1,131,566 options available for issuance under the Plan. The amount of options available

for issuance will change as we grant options in 2008 and as the actual number of common shares outstanding changes as well.

During the second quarter of 2008, the combination of vesting of existing options and the recognition of options cancelled resulted in a net compensation cost of \$36. In addition, during the second quarter of 2008, no options were exercised to purchase common shares and 193,828 options were cancelled or expired.

Warrants

In the three months ended June 30, 2008, the Company issued 9,300,000 common share purchase warrants with a value of \$576, no common share warrants were exercised and no common share purchase warrants expired. As at June 30, 2008 there were 9,300,000 (\$0.09 exercise price) warrants to purchase common shares outstanding.

We increased our contributed surplus from \$9,039 to \$9,075 for the three months ended June 30, 2008 as a result of the inclusion as an equity item \$36 recognized as stock option compensation costs in the consolidated statement of operations.

Six months

Stock Options

During the six months ended June 30, 2008, \$1,298,986 options were granted to employees (all in the second quarter) to purchase shares of the company under the stock options incentive plan.

During the first quarter of 2008, the combination of vesting of existing options and the recognition of options cancelled resulted in a net compensation cost of \$72. In addition, during the first six months of 2008, no options were exercised to purchase common shares and 289,503 options were cancelled or expired.

Warrants

In the six months ended June 30, 2008, 9,300,000 common share warrants were issued (all in the second quarter); while no common share warrants were exercised and there were 250,000 common share warrants that expired. As at June 30, 2008 there were 9,300,000 (\$0.09 exercise price) warrants to purchase common shares outstanding.

We increased our contributed surplus from \$8,941 at December 31, 2007 to \$9,075 as at June 30, 2008 as a result of the inclusion as an equity item the net of the following three items: first, an increase of \$72 recognized as stock option compensation costs in the consolidated statement of operations and second, an increase of \$62 as a result of the expiration and cancellation of warrants to purchase common shares whose value was transferred from share capital.

27. OUTSTANDING SHARE DATA

The following table summarizes the changes in the common shares, common share purchase warrants and options to purchase common shares for the six months ended June 30, 2008.

	Common Shares	Warrants	Options
Outstanding at December 31, 2007	55,993,929	250,000	6,258,040
Issued / Exercised	-	-	-
Granted	-	9,300,000	1,298,986
Cancelled / Expired	-	(250,000)	(289,503)
Outstanding at June 30, 2008	55,993,929	9,300,000	7,267,523

As at June 30, 2008, there were 9,300,000 common share purchase warrants outstanding at an exercise price of \$0.09.

As at June 30, 2008, there were 7,267,523 stock options outstanding at exercise prices ranging from \$0.11 to \$0.68 with expiry dates from January 20, 2010 through June 28, 2012.

28. OFF-BALANCE-SHEET ARRANGEMENTS

In the normal course of business we may be required to issue letters of credit or performance guarantees. As at June 30, 2008, we had one outstanding letter of credit with a Canadian financial institution in the amount of \$615 (2007 – nil). This relates to our contract to provide a CPT to the RDAF via prime contractor AgustaWestland. The collateral on the letter of credit was changed in August 2007 from cash to a guarantee issued by Export Development Canada.

29. ACCOUNTING POLICY DEVELOPMENTS

We may use foreign exchange forward contracts to manage exposures created when sales and purchases are made in foreign currencies. As at June 30, 2008, there were no foreign exchange forward contracts outstanding (2007 - nil).

We do not use derivative instruments to reduce our exposure to interest rate risk or to change our exposure from fixed to floating interest rates. The interest rate floats on the credit facility, of which US\$2,000 was utilized as of June 30, 2008 (2007 – nil) and on the Term Loan the interest rate is fixed.

30. RELATED PARTY TRANSACTIONS

All related party transactions are in the normal course of operations, measured at their exchange amounts established and agreed to by the related parties. Amounts due to related parties are subject to normal trade terms. In the three months and six months ending June 30, 2008, the Company paid the following amounts to firms in which a director of the Company is an owner, partner or principal: \$75 and \$278 respectively (2007 - \$62 and \$316) for legal services. The cost of these services was charged to the Comvest term loan account as well as to general and administrative expenses. The amount due to related parties included in accounts payable and accrued liabilities as at June 30, 2008 was \$213 (2007 - \$119).

31. CRITICAL ACCOUNTING ESTIMATES

We are required to make estimates and assumptions when accounting for assets and liabilities and when disclosing contingent assets and liabilities at the date of the financial statements and for revenues and expenses for the period reported. We regularly review and change, when necessary, our estimates and assumptions, particularly as they relate to accounting for long-term contracts, stock-based compensation costs, income taxes, deferred development costs and goodwill, based on management's judgment of current conditions and actions that we may undertake in the future. Actual results may differ from estimates previously recorded.

32. BUSINESS OUTLOOK

The following contains forward-looking statements about our business outlook for 2008. Reference should be made to "Forward-Looking Statements" on page 5. For a description of material factors that could cause our actual results to differ materially from the forward-looking statements in the following, please see the Business Risk Factors section of this MD&A on page 32 and the Description of the Business – Risk Factors section in our Annual Information Form.

Our profitability in the short term will be determined by the uncertain timing of military contracts. We have acquired Eduplus to increase our e-learning capability and access to Canadian naval opportunities. We intend to expand our penetration of the Canadian energy industry and begin planting the seeds for a more global energy sector strategy. We plan to conduct field trials on HVTT in the third quarter of the year. We anticipate additional business from the CFTS program and to close on a number of other contracts in the second half of the year.

We expect that:

- Approximately \$6 million to \$8 million of our order backlog as at June 30, 2008 of \$32.1 million will be realized as revenue in the remainder of 2008. Our ability to replenish our backlog in the last half of 2008 will be a key determinant of our outlook for 2008.
- Revenues from the initial contract under the CFTS program for 2008 will decrease compared to 2007, however, we are pursuing additional opportunities under the CFTS program. As at June 30, 2008, approximately \$2.4 million of revenue remained to be recognized for the initial phase of the project. We believe that the CFTS program has contributed significantly to our intellectual property and has enhanced our ability to handle large and complex learning systems. In addition, our participation in the program greatly enhances our ability to capture significant new business that will flow from the CFTS program in the form of enhancements to the existing program and new procurement programs. As a result, we believe that the CFTS program and related opportunities will continue to be a significant contributor to our Company's revenue base for the foreseeable future due to planned and projected upgrades, enhancements and improvements to the training procedures and technologies required by the CF throughout the life cycle of the program.

- Gross margins will continue to fluctuate and will depend on our future revenue base, the mix of lower margin CFTS revenue relative to higher margin projected new business and our ability to manage fixed costs.
- The Company has filed for \$1.2 million in cash tax credits, net of fees, on 10 separate projects with the Ontario Media Development Corporation for Ontario Interactive Digital Media Tax Credits. In order to access these cash tax credits the Company must obtain certificates of eligibility from the Ontario Media Development Corporation and hopes to do so before December 31, 2008.
- Our cost reduction plan will reduce overall operating expenses by approximately 15% and will provide in 2008 savings of approximately \$4.0 million
- Depreciation and amortization expense will increase in 2008 as compared to 2007 due to the full year of amortization of the HVTT and the core technology acquired in the Eduplus transaction.
- General and administrative and sales and marketing expenses are planned to decrease in 2008 as a result of our cost reduction plan.
- Interest expense and financing costs will increase significantly over 2007 levels due to the outstanding term loan and revolving line of credit secured in April 2008.
- Cash and cash equivalents will likely to decline as additional losses are expected for the balance of the year.. Cash availability to fund future operations will be dependent on the Company's ability to secure new orders and its ability to secure additional capital..
- Although we have as of May 2008 repaid our bank term loan and replaced it with a three-year term loan, unanticipated outflows in 2008 and future out of covenant events that may not be waived by the lender may result in our need to complete additional financings. Access to such capital at acceptable commercial terms for a company of our size and financial status will be greatly dependent on our ability to increase our backlog position, demonstrate execution of our business strategy and the general condition of the credit markets and may be significantly dilutive to existing shareholders.
- Capital expenditures, without giving effect to assets acquired in acquisitions, will be comparable to 2007 levels.

33. REPORT ON DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") are responsible for establishing and maintaining the Company's disclosure controls and procedures. They are assisted in this responsibility by the Company's Disclosure Committee, which consists of senior managers of the Company. The Disclosure Committee evaluates material information to determine the appropriateness and timing of its public release. The CEO and CFO have evaluated the effectiveness of the Company's disclosure controls and procedures and have concluded that they were adequate and effective as of June 30, 2008.

The Company maintains internal controls over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of financial statements in accordance with generally accepted accounting principles. The Company's CEO and CFO do not expect that these internal controls will prevent all error and all fraud. Internal controls can only provide reasonable, not absolute, assurance that the objectives of the system are met. Because of inherent limitations, internal controls over financial reporting may not prevent or detect misstatements and fraud. Controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the control. Internal controls over financial reporting are based partly on assumptions about the likelihood of future events and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

During the three months ended June 30, 2008, there have been no changes in our Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our Company's internal control over financial reporting.

34. BUSINESS RISK FACTORS

Our operations and financial results are subject to various risks and uncertainties which are outlined below. These risks are in addition to those outlined elsewhere in this MD&A and in our Annual Information Form.

New Contracts

The Company anticipates securing significant new projects in the last two quarters of 2008 by successfully completing ongoing negotiations with new and existing customers for new work. However, there can be no assurance that the expected new contracts will close in this period and an inability to do so will significantly affect our consolidated results of operations and financial condition.

Financing

Our future is dependent on management's ability to secure capital in the current marketplace on reasonable terms for a company of our size and financial status. There can be no assurance that we will secure required capital and an inability to do so would negatively affect our financial condition.

Limited Financial Resources

The Company's financial resources are currently limited. There can be no assurance that this will not negatively affect our ability to obtain or execute contracts, including our ability to obtain letters of credit or performance bonds or meet working capital requirements.

Reliance on Key Customers

In any one fiscal year, we have typically derived a substantial portion of our revenues from a small number of contracts with major customers. Historically, one customer in particular has represented a substantial portion of our revenues. The composition of this group of major customers may change from year to year and our revenues and profitability are dependent upon our ability to win key contracts from such major customers, and then successfully execute such contracts, which represents substantial business and credit risk concentration.

Availability of Skilled Personnel

Our performance depends on our ability to attract and retain personnel with appropriate technical, administrative and program-related skills and experience. To the extent that we are unable to attract and retain such personnel, our competitiveness could be adversely affected. Our cost reduction plan may adversely affect our ability to retain key personnel.

Performance of Contracts and Dependence on Subcontractors

We are dependent on our ability to meet contractual obligations under the CFTS program or any other major program. We are also dependent on completing these projects on time and on budget. Furthermore, our ability to meet contractual obligations and complete projects on time and on budget is dependent on the performance of our subcontractors, as well as the relative proportion of in-house and subcontractor work. There can be no assurance that we will meet our contractual commitments or complete projects within our budget and failure to do so may negatively affect our consolidated results of operations, our financial condition and our ability to obtain subsequent work.

Cost Reduction Program

We have implemented a cost reduction plan. There can be no assurance that the program will be fully implemented in the timeframe expected and failure to do so may have a negative affect on our consolidated results of operations and financial condition.

Timing of Revenue Recognition from Backlog

A delay from the Company's expectations of when it will recognize revenue from its current order backlog may have a negative affect on our consolidated results of operations and financial condition.

Level of Military Expenditures

There is no assurance that management's expectations as to the stability and growth of military markets and expenditures worldwide will materialize. There can also no assurance that management's expectations of the acceptance of our product offerings by the energy and aerospace industries will materialize. To the extent there is a significant change from these expectations, our consolidated results of operations and our financial condition may be negatively affected.

Length of Sales Cycles

The nature of our business involves lengthy sales cycles and regular delays over which we have no control. Any ongoing failure to achieve such sales could have a material adverse effect on our business, financial condition and the results of our operations. Furthermore, maintenance of our key partnerships as our sales strategies evolve is essential.

Reliability of Cost Estimates

Revenue and profitability initially recognized on our long-term contracts depends on reliable cost estimates made in the early stages of such projects. To the extent that there is a significant change in these cost estimates, our revenue and profitability in subsequent periods could change significantly which could, in turn, have an adverse affect on our consolidated results of operations and on our financial condition.

Ownership of Technology

Our future is dependent on management's ability to protect and exploit our intellectual property. We rely in part on trade secrets and contractual arrangements, such as confidentiality and non-disclosure agreements, to establish and protect our technology. Such reliance may be insufficient to prevent misappropriation of our technology or to deter others from developing similar technologies. Enforcement of our intellectual property rights or our ability to acquire such rights may be unavailable or limited. In addition, infringement claims may be brought against us or our customers in the future. We may not be successful in the defence of such claims and may not be able to develop processes that do not infringe on the rights of third parties or obtain licenses on commercially acceptable terms, if at all.

HVTT Acceptance

There can be no assurance that our forecasted sales of the HVTT product will materialize. Significantly lower HVTT sales could adversely affect operating results and may require that we accelerate the write down of the carrying value of this initiative.

Technological Change

The markets for our current and planned products and services are characterized by rapid technological advances, competing technological platforms, emerging and evolving industry standards, changes in customer requirements and frequent new product introductions and enhancements. Our future success will depend upon our ability to enhance our current products and services, develop and introduce new products and services that keep pace with technological developments, respond to evolving customer requirements, meet the technical requirements of our strategic partners and achieve market acceptance for our products. We rely on technological competence to provide value to our customers. In an environment of rapid technological change, ownership of any particular technology cannot guarantee market position. To the extent that we are unable to sustain our technological competitiveness, we may be less successful in achieving future contract awards.

Foreign Exchange

Fluctuations in the value of the Canadian dollar relative to foreign currencies (particularly the US dollar), could result in exchange gains and losses or increased costs.

US Subsidiary

ASA's projected expense levels are based on the assumption that we will win additional contracts in the US. Should we be unable to win additional contracts and reduce ASA spending accordingly, ASA expense levels will negatively affect our consolidated results of operations and financial condition.

Growth of Simulation Training Markets

There is no assurance that management's expectations as to the stability and growth of markets for simulation-based training products will materialize. To the extent there is a significant change from these expectations, our consolidated results of operations and our financial condition may be negatively affected.

Goodwill

To the extent that prospects for profitability and operating cash flows are not realized, we will face a possible impairment to the carrying value of our goodwill, requiring a charge to be taken against our operating results.

Acquisitions

We may pursue acquisitions in order to complement or expand our business. The negotiation of potential acquisitions could divert our time and resources and require funds to consummate. The process of combining with another company could be disruptive to our business and could result in unforeseen operating difficulties requiring financial resources. Further, we may finance future acquisitions through borrowings or otherwise incur indebtedness in connection with acquisitions. In addition, if we consummate one or more acquisitions through the issuance of common shares, holders of common shares could suffer dilution of their ownership interests.

Regulatory Compliance

We are subject to laws, regulations and standards relating to corporate governance and public disclosure in Canada. Our efforts to comply with such requirements have resulted in, and may continue to result in, increased general and administrative expenses and diversion of management time and attention from revenue-generating activities to compliance activities. Recently, we completed our first assessment of our internal controls over financial reporting with a view to being able to conduct an evaluation when requirements to do so are imposed by Canadian securities regulators in the future. In assessing ASA, we have identified that proper segregation of duties does not exist due to its start-up nature. Such assessment of our internal controls over financial reporting is a continuing process and may bring to light additional weaknesses in internal control over financial reporting. To the extent that we identify additional internal control weaknesses that require correction, we may be required to incur expenditures or costs, which, if significant, could adversely affect our operating results.

Relationship with Existing US Prime Contractors

Certain opportunities in the United States will require continued business relationships with our partners who are prime contractors for US military procurements. If we are unable to maintain and develop these relationships, business opportunities in the United States may be limited which could, in turn, have an adverse affect on our consolidated results of operations and on our financial condition.

Commitments

As a condition of dispositions, teaming agreements and in the normal course of our business, we enter into non-compete, non-disclosure, and other similar commitments. Non-performance on these commitments could negatively affect future results.

Change to Canadian Government Policies

Our historical operating results reflect substantial benefits from programs sponsored by the Canadian government to support businesses like ours. If changes in law or government policies regarding these programs were to result in their termination or adverse modification, or if we were to become unable to participate in, or take advantage of these programs, the

cost of our operations could materially increase and there could be an adverse effect on our results.

Competition

The markets in which we operate are highly competitive. Competition may prevent us from winning significant contracts and may prevent us from realizing historically typical levels of profitability. Any such effects would negatively affect our consolidated results of operations and financial condition.

Additional information about us can be found in our Annual Information Form and in our Management Information Circular, both of which are available on SEDAR at www.sedar.com.

August 14, 2008

Interim Consolidated Financial Statements of

ATLANTIS SYSTEMS CORP.

June 30, 2008 and 2007

Interim Consolidated Financial Statements of

ATLANTIS SYSTEMS CORP.

June 30, 2008 and 2007

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ATLANTIS SYSTEMS CORP.**Consolidated Statements of Operations, Comprehensive Loss and Deficit****For the three months and six ended June 30****(Expressed in thousands of Canadian dollars except per share amounts)**

	For the three months ended June 30		For the six months ended June 30	
	2008 (unaudited)	2007 (unaudited)	2008 (unaudited)	2007 (unaudited)
Revenue (Notes 6, 14)	\$ 4,245	\$ 15,241	\$ 8,584	\$ 21,070
Cost of revenue (Note 12)	3,831	9,736	8,023	14,339
Gross margin	414	5,505	561	6,731
Expenses				
General and administrative	1,416	1,935	2,854	3,932
Selling and marketing	468	735	835	1,647
Stock options	36	60	72	102
	1,920	2,730	3,761	5,681
Operating (loss) income before the undernoted items	(1,506)	2,775	(3,200)	1,050
Depreciation and amortization	522	171	1,052	324
Interest and financing costs (income), net (Note 8)	309	(67)	387	(169)
Gain on disposal of capital assets	-	-	-	(1)
Net (loss) income and comprehensive (loss) income	(2,337)	2,671	(4,639)	896
Deficit, beginning of period	(81,265)	(76,706)	(78,963)	(74,931)
Deficit, end of period	\$ (83,602)	\$ (74,035)	\$ (83,602)	\$ (74,035)
Net (loss) income per share (Note 13)				
Basic and diluted	\$ (0.04)	\$ 0.05	\$ (0.08)	\$ 0.02
Diluted	\$ (0.04)	\$ 0.05	\$ (0.08)	\$ 0.02
Weighted average number of shares				
Basic and diluted	55,993,929	54,699,431	55,993,929	54,152,990
Diluted	55,993,929	55,440,870	55,993,929	55,163,936

The accompanying notes are an integral part of these consolidated statements.

ATLANTIS SYSTEMS CORP.
Consolidated Balance Sheets

(Expressed in thousands of Canadian dollars)

	June 30 2008 (unaudited)	December 31 2007
ASSETS		
Current assets		
Cash and cash equivalents (note 9)	\$ 923	\$ 3,720
Trade and other receivables (Note 6)	2,188	2,766
Unbilled revenue	2,770	2,453
Inventory	516	510
Mortgage Receivable	249	249
	6,646	9,698
Capital assets, net	1,402	1,671
Other long-term assets	216	235
Mortgage receivable	158	150
Deferred development costs and core technology, net (Note 7)	3,642	4,382
Goodwill	11,735	11,735
	17,153	18,173
	\$ 23,799	\$ 27,871
LIABILITIES		
Current liabilities		
Operating line of credit	\$ 2,039	\$ -
Accounts payable and accrued liabilities	3,229	4,601
Accrued costs on percentage completion	444	301
Deferred revenue	973	954
Term debt (Notes 9, 11)	1,751	2,660
	8,436	8,516
SHAREHOLDERS' EQUITY		
Share capital (Notes 10, 11)	89,890	89,377
Contributed surplus	9,075	8,941
Deficit	(83,602)	(78,963)
	15,363	19,355
	\$ 23,799	\$ 27,871

The accompanying notes are an integral part of these consolidated statements.

ATLANTIS SYSTEMS CORP.
Consolidated Statements of Cash Flows
For the three and six months ended June 30
(Expressed in thousands of Canadian dollars)

	For the three months ended June 30		For the six months ended June 30	
	2008 (unaudited)	2007 (unaudited)	2008 (unaudited)	2007 (unaudited)
Cash flows provided by (used in) :				
Operating activities :				
Net (loss) income	\$ (2,337)	\$ 2,671	\$ (4,639)	\$ 896
Items not affecting cash:				
Depreciation and amortization	522	171	1,052	324
Gain on disposal of capital assets	-	-	-	(1)
Stock options expensed	36	60	72	102
Accretion on term debt	70	-	70	-
	(1,709)	2,902	(3,445)	1,321
Interest on mortgage receivable	(4)	(3)	(8)	(7)
Other long-term assets	13	(141)	11	(138)
Net change in non-cash working capital (Note 15)	925	(8,032)	(955)	(11,787)
	(775)	(5,274)	(4,397)	(10,611)
Investing activities :				
Investment in capital assets	(16)	(192)	(36)	(355)
Proceeds from disposal of capital assets	-	-	-	1
	(16)	(192)	(36)	(354)
Financing activities :				
Old term debt repayment (Note 9)	(2,520)	-	(2,660)	-
New term debt (Note 9)	2,257	-	2,257	-
Exercise of common share purchase warrants	-	-	-	873
Exercise of options to common shares	-	-	-	108
	(263)	-	(403)	981
Net decrease in cash and cash equivalents	(1,054)	(5,466)	(4,836)	(9,984)
Cash and cash equivalents, beginning of period	(62)	9,118	3,720	13,636
(Bank indebtedness) cash and cash equivalents, end of period	\$ (1,116)	\$ 3,652	\$ (1,116)	\$ 3,652

SUPPLEMENTAL INFORMATION

(Bank indebtedness) cash and cash equivalents are comprised of:

Cash	\$ 923	\$ 3,621	\$ 923	\$ 3,621
Cash equivalents	-	31	-	31
Bank operating line of credit	(2,039)	-	(2,039)	-
	\$ (1,116)	\$ 3,652	\$ (1,116)	\$ 3,652
Interest paid	\$ 124	\$ 3	\$ 172	\$ 5
Income taxes paid	\$ -	\$ -	\$ -	\$ -

The accompanying notes are an integral part of these consolidated statements.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

June 30, 2008 and 2007

(Expressed in thousands of Canadian dollars except per share amounts, unless otherwise indicated)

1. BASIS OF PRESENTATION

Atlantis Systems Corp. (“Atlantis” or the “Company”) continued under the laws of Canada and is listed on the Toronto Stock Exchange (TSX-AIQ). Atlantis Systems International Inc. (“ASI”) and Atlantis Systems America Inc. (“ASA”) are operating subsidiaries of the Company. ASI is a training integrator specializing in military, commercial aviation and energy markets worldwide. ASI combines desktop and full-flight simulation, knowledge management, learning management systems and multimedia courseware to provide integrated training systems to customers. ASA has been established to provide similar services in the United States. In addition, the Company has an 85% interest in Denbridge Digital Limited, which is an inactive holding company.

2. INTERIM FINANCIAL STATEMENT PREPARATION

The disclosures in these interim unaudited consolidated financial statements do not meet all disclosure requirements of Canadian generally accepted accounting principles for annual financial statements. These interim unaudited consolidated financial statements should be read in conjunction with the annual financial statements of the Company and the notes thereto. Except as explained in Note 3, the interim unaudited consolidated financial statements are prepared using the same accounting principles and application thereof as the annual financial statements for the year ended December 31, 2007. Note disclosures have been presented for material updates to the information previously reported.

3. CHANGE IN ACCOUNTING POLICIES

On January 1, 2008, the Company adopted the recommendations of CICA Handbook Section 3031, Inventories. This Section provides guidance on the measurement and disclosure requirements for inventories. The adoption of this new Section did not have an impact on the Company’s financial results.

4. FUTURE ACCOUNTING CHANGES

International Financial Reporting Standards

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

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

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

June 30, 2008 and 2007

(Expressed in thousands of Canadian dollars except per share amounts, unless otherwise indicated)

4. FUTURE ACCOUNTING CHANGES (continued)

International Financial Reporting Standards(continued)

As the International Accounting Standards Board currently, and expectedly, has projects underway that should result in new pronouncements that continue to evolve IFRS. As of the date of these unaudited consolidated financial statements, the financial reporting impact of the transition to IFRS cannot be reasonably estimated.

Goodwill and Intangibles

In February 2008, the CICA issued Handbook Section 3064, Goodwill and Intangible Assets, which establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. CICA Handbook Section 1000, Financial Statement Concepts, was also amended to provide consistency with this new standard. The new and amended standards are effective for the Company beginning January 1, 2009. The Company is currently assessing the impact of these standards on its financial statements.

5. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of the Company are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The significant accounting policies are as follows:

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated on consolidation for subsidiaries.

Revenue recognition

Revenue from long-term contracts for developing, building and supporting simulators and training systems is recognized using the percentage of completion method where revenue is recorded as labour costs are incurred, based on actual labour costs incurred to date on a contract, relative to the estimated total labour costs to complete the contract. When subcontractor or material costs form a significant portion of total costs, revenue is recognized as costs are incurred based on labour, material and actual sub-contract costs incurred to date on a contract, relative to the estimated total labour, material and sub-contract costs to complete the contract. In the event that the Company has large contracts where it can segment costs into separate sub-components, revenue is recognized as each sub-component progresses to completion. All other revenues and related costs are recorded at the time the services are performed or the product is delivered. Full provision is made for any anticipated losses in the period in which the relevant facts become known.

Unbilled revenue represents revenue earned in excess of amounts billed on uncompleted contracts. Deferred revenue represents the extent that billings to clients are in excess of revenue recognized to date. The results reported under the percentage of completion method are based on the Company's estimates of total labour and sub-contract costs to complete the various contracts. Should total actual

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

June 30, 2008 and 2007

(Expressed in thousands of Canadian dollars except per share amounts, unless otherwise indicated)

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition (continued)

labour or sub-contract costs be materially higher or lower than these estimates, adjustment to future results would be necessary.

Disputes arise in the normal course of the Company's business on projects where the Company contests with customers or owners for additional funds because of events such as delays or changes in contract specifications. Such disputes, whether claims or unapproved changes in process of negotiation, are recorded at the lesser of their estimated value or actual costs incurred and only when realization is certain. Claims against the Company are recognized when the loss is considered probable and reasonably determinable.

The Company follows the accounting recommendations of Emerging Issues Committee ("EIC") EIC-141 "Revenue Recognition", EIC-142, "Revenue Arrangements with Multiple Deliverables" and EIC-143, "Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts". EIC-141 summarizes the principles set as interpretive guidance on the application of

CICA Handbook section 3400, "Revenue". Specifically this EIC presents the criteria to be met for revenue recognition to be considered achieved. EIC-142 addresses certain aspects of the accounting by a vendor for arrangements under which it will perform multiple revenue generating activities for a given customer. Finally, EIC-143 considers the issue of how revenue and costs from separately priced extended warranty or product maintenance contracts should be recognized. The Company currently has contracts that include multiple deliverables as defined in EIC-142. For each of these contracts, the delivered item does not qualify as a separate unit of accounting. As a result, the consideration allocable to the delivered item is combined with the consideration allocable to the undelivered item and revenue recognition is determined on the combined deliverables as a single unit of accounting.

Research and development costs

Research costs, net of related investment tax credits, are expensed as incurred. Development costs, net of related investment tax credits, are expensed as incurred unless such costs meet the criteria for deferral and amortization under Canadian GAAP.

Deferred development costs

The Company's policy is to expense development costs unless they meet generally accepted criteria for capitalization. These criteria include whether the product is clearly defined, attributable costs can be identified, technical feasibility has been established, the market for the product has been clearly defined and management intends to pursue that market and sufficient resources exist to complete the project. Upon commercial launch of the product, these costs are to be amortized over the number of unit sales, over a period not to exceed forty-eight months. The Company assesses the recoverability of the capitalized costs by determining whether the unamortized balance can be recovered through undiscounted projected future net cash flows of the related products. The benefits of investment tax credits are recognized as a reduction of development expenditures in the period the qualifying expenditures are incurred if there is reasonable assurance the tax credits will be realized.

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5. SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments

(a) Financial assets and financial liabilities

Financial assets and financial liabilities are initially recognized at fair value and are subsequently accounted for based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Except in very limited circumstances, the classification is not changed subsequent to initial recognition.

Held for trading

Financial assets that are purchased and incurred with the intention of selling or repurchasing in the near term are classified as held for trading. These instruments are accounted for at fair value with changes in the fair value recognized in net income during the period. Cash and cash equivalents are classified as held for trading.

Available-for-sale

Financial assets classified as available-for-sale are carried at fair value with any gains or losses arising from changes in fair value recorded in other comprehensive income (loss). When a decline in fair value is determined to be other-than-temporary, the cumulative loss included in accumulated other comprehensive income is removed and recognized in net income (loss). Gains and losses realized on disposal of available-for-sale securities are recognized in other income. No investments are classified as available-for-sale.

Held-to-maturity

Securities that have a fixed maturity date and which the Company has positive intention and the ability to hold to maturity are classified as held-to-maturity and accounted for at amortized cost using the effective interest rate method. No investments are classified as held-to-maturity.

Loans and Receivables

Trade and other receivables and the mortgage receivable are classified as loans and receivables, which are measured at amortized cost.

Other financial liabilities

Accounts payable and accrued liabilities, and the term debt are classified as other financial liabilities, which are measured at amortized cost using the effective interest rate method.

(b) Embedded derivatives

Derivatives may be embedded in other financial and non-financial instruments (the “host instrument”). Embedded derivatives are treated as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host instrument, the terms of the embedded derivative are the same as those of a stand-alone derivative, and the combined contract is not held for trading or designated at fair value. Embedded derivatives are measured at fair value with subsequent changes recognized in the Statement of Operations, Comprehensive Loss and Deficit as an element of general and administrative expenses.

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5. SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Determination of fair value

The fair value of a financial instrument on initial recognition is the transaction price, which is the fair value of the consideration given or received. Subsequent to initial recognition, fair value is determined by using valuation techniques which refer to observable market data.

(d) Comprehensive income (loss)

Comprehensive income is composed of the Company's net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on available-for-sale securities, net of income taxes. The components of comprehensive income (loss) are disclosed in the Consolidated Statement of Operations, Comprehensive Loss and Deficit. The Company does not currently have any other comprehensive income (loss).

Foreign currency translation

The Company's foreign subsidiary is considered to be an integrated operation and its accounts are translated into Canadian dollars using the temporal method. The temporal method is also applied to monetary assets and liabilities of the Company, as well as revenue and expenses, which are denominated in foreign currencies. Under this method, monetary items are translated at the rate of exchange at the balance sheet dates, non-monetary items are translated at historical exchange rates and revenues and expenses are translated at the average exchange rate for the year. Amortization of non-monetary assets is translated at the same exchange rate as the assets to which they relate.

Exchange gains or losses on translation are included in the determination of the net income (loss) for the year.

From time to time, the Company enters into forward foreign exchange contracts to manage exposures resulting from foreign exchange fluctuations in the ordinary course of business. Gains and losses on these contracts are deferred and accounted for as part of the transactions being hedged, when the criteria established by AcG-13 are met. The Company negotiates forward contracts only with financially sound counter parties. During the six months ended June 30, 2008, the Company did not enter into any forward contracts and did not have any contracts outstanding.

Cash and cash equivalents

Cash and cash equivalents include deposits and other highly liquid financial instruments all having a maturity of 90 days or less from the date of purchase.

Inventory

Inventory of finished goods, work-in-process, and raw materials are recorded at the lower of cost, determined on a first-in, first-out basis, and net realizable value. The cost of work in process includes material, labour, and an allocation of manufacturing overhead.

Capital assets

Capital assets are recorded at cost, net of any investment tax credits, and are amortized on a straight-line and declining balance basis over the estimated useful lives of the related assets, at annual rates between 20% and 30%.

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5 SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of long lived assets

Long lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. An impairment loss is recognized when the carrying amount of a long lived asset is not recoverable and exceeds its fair value.

Goodwill

Goodwill represents the excess of the purchase price paid to acquire a business over the fair value of its underlying net identifiable assets. Goodwill is not amortized. The Company reviews the valuation of goodwill on an annual basis or when an event or circumstance occurs which more likely than not reduces the fair value of a reporting unit below its carrying amount. In doing so, the Company evaluates whether there has been impairment in the value of goodwill based on a comparison of the fair value of the reporting unit to the underlying carrying value of the reporting unit's net assets, including goodwill. Discounted cash flows are used to determine the fair value of the reporting unit.

Capital disclosure

On October 1, 2007, the Company adopted the CICA Handbook Section 1535 for Capital Disclosures. This accounting standard requires the disclosure of the Company's objectives, policies and processes for managing capital as discussed further in Note 12.

Stock-based compensation plans

The Company has a stock-based compensation plan for directors, officers, employees and consultants. All stock options granted under the plan have an exercise price not less than the market price of the shares on the date the option is granted. The Company utilizes the fair-value method of accounting for stock-based compensation awards. Under this policy, the Company determines the fair value of the stock options on the grant date and records the fair value as a compensation expense over the period that the stock options vest, with a corresponding increase to contributed surplus. When these options are exercised, the amount of proceeds, together with the amount recorded in contributed surplus are recorded in share capital. The fair value of these options are determined using the Black-Scholes option pricing model.

Severance and termination benefits

The Company has applied the guidance in Emerging Issue Committee EIC 134, Accounting for Severance and Termination Benefits, to employee severance or termination benefits, and in particular, to the Company's cost reduction plan which commenced implementation in 2007. This interpretative guidance is used to supplement the application of CICA Handbook section 3461, Employee Future Benefits.

The Company has concluded that the employee future benefits arising from its cost reduction plan were severance benefits and accordingly, these costs of approximately \$802 were accrued and

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5 SIGNIFICANT ACCOUNTING POLICIES (continued)

expensed in the fourth quarter of 2007. As at June 30, 2008 the Company has \$306 of the accrual remaining.

Income taxes

The Company uses the asset and liability method for accounting for income taxes. Under this method, temporary differences between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using substantively enacted tax rates anticipated to apply in the periods that the temporary differences are expected to reverse. The effect of the change in income tax rates on recognized future income tax liabilities or assets is recognized in income in the period that the change occurs. Future income tax assets are evaluated annually and if realization is not considered more likely than not, the value of the recognized future tax asset is adjusted by a charge to income.

Use of estimates

The preparation of consolidated financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions. These estimates affect the reported amounts of assets and liabilities and disclosures of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates used in the financial statements include the following: revenue recognition and estimated costs to complete for percentage of completion basis on long-term contracts; allowance for doubtful accounts and inventory reserves; valuation of goodwill and long-lived assets; provision for product warranties and estimates used in the valuation of stock options. Actual results could differ from those estimates.

Earnings per share

Basic earnings per share is computed using the weighted average number of common shares outstanding during the year. Diluted earnings per share is computed using the weighted average number of common and potential common shares outstanding during the year. Potential common shares consist of the incremental common shares issuable upon the exercise of stock options and share purchase warrants that are dilutive to the earnings per share calculation. The weighted average number of potential common shares issuable upon the exercise of stock options and share purchase warrants is calculated using the treasury stock method.

Variable interest entities

During 2005, the Company adopted Accounting Guidelines 15 ("AcG-15"), Consolidation of Variable Interest Entities ("VIEs"). AcG-15 provides criteria for the identification of VIEs and further criteria for determining what entity, if any, should consolidate them. AcG-15 defines a VIE as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the equity investors lack the characteristics of a controlling financial interest. VIEs are subject to consolidation by the Company if it is deemed the primary beneficiary of the VIE. The primary beneficiary is the party that is either exposed to a majority of the expected losses from the VIE activities or is entitled to receive a majority of the VIE residual returns or both. The Company has determined that it is not the primary beneficiary of any VIE.

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6. CONCENTRATION OF CREDIT RISK

The Company has contracts with many customers; however, as at June 30, 2008 two customers each represented 38% and 35% of the accounts receivable and unbilled revenue respectively (December 31, 2007 – 35% and 29%) and a different customer represented 15% while the second customer represented 45% of revenue for the three months ended June 30, 2008 (2007 – 0% and 88%) and 14% and 43% of revenues for the six months ended June 30, 2008 (2007 – 0% and 79%).

The following table summarizes the value of assets included in trade and other receivables:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Trade receivables	\$ 1,849	\$ 2,298
Other receivables	339	468
	<u>\$ 2,188</u>	<u>\$ 2,766</u>

7. DEFERRED DEVELOPMENT COSTS AND CORE TECHNOLOGY

The following table summarizes the value of assets included in deferred development costs:

	<u>2008</u>		
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
HVTT deferred development costs	\$ 1,669	\$ 418	\$ 1,251
Eduplus core technology	3,188	797	2,391
	<u>\$ 4,857</u>	<u>\$ 1,215</u>	<u>\$ 3,642</u>
	<u>2007</u>		
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
HVTT deferred development costs	\$ 1,669	\$ 209	\$ 1,460
Eduplus core technology	3,188	266	2,922
	<u>\$ 4,857</u>	<u>\$ 475</u>	<u>\$ 4,382</u>

In 2006, the Company continued to fund a specific development project focused on the Helicopter Virtual Task Trainer (HVTT) concept. No development costs were capitalized in 2007 or during the six months ended June 30, 2008. There are sufficient identified markets and forecasted sales of the \

HVTT product to recover the costs capitalized and generate profits. Amortization for the HVTT commenced in the third quarter of 2007.

Eduplus core technology is software that was acquired as part of the purchase of the Eduplus division of Tecsuit Inc. on September 27, 2007 and is being amortized over three years.

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8. INTEREST AND FINANCING COSTS (INCOME)

	For the three months ended		For the six months ended	
	June 30		June 30	
	2008	2007	2008	2007
Interest expense	\$ 193	\$ 3	\$ 241	\$ 5
Finance and bank charges	128	1	179	6
Interest income	(12)	(71)	(33)	(180)
	<u>\$ 309</u>	<u>\$ (67)</u>	<u>\$ 387</u>	<u>\$ (169)</u>

9. OPERATING LINE OF CREDIT AND RESTRICTED CASH

On April 30, 2008, the Company entered into financing arrangements with ComVest Capital LLC (ComVest") that provided up to US\$6,600 of financing in the form of a secured term loan (the "New Term Loan") in the amount of US \$2,600 at a rate of interest of 12.5% per annum payable monthly and a deferred interest fee of 5% per annum payable at maturity as well as a secured revolving line of credit (the "Line of Credit") of up to US\$4,000 based on a borrowing base at a rate of interest of US prime plus 2% per annum with a floor of 8%. The New Term Loan matures on April 30, 2011 and the Line of Credit will be available until April 30, 2010, subject to a one-year extension at the option of the Company. These financing arrangements closed on May 5, 2008 and the New Term Loan was used to repay the term loan secured from the Company's creditors in the third quarter of 2007. The arrangement also involved the Company issuing warrants to acquire an aggregate of 9,300,000 common shares at an exercise price of \$0.09 per share for a period of five years.

The Company has available a general operating line of credit up to US\$4,000 of which US\$2,000 was utilized as of June 30, 2008 (2007 – nil). The line of credit bears interest at a rate of US prime lending rate plus 2% with a floor of 8%. The line of credit is collateralized by a general security agreement over all present and future personal property.

In July 2006, as a condition of a new contract to provide a cockpit procedures trainer, the Company entered into a letter of credit with a Canadian financial institution in the amount of \$2,051. The collateral on the letter of credit was changed in August 2007 from cash to a guarantee issued by Export Development Canada. The value of this letter of credit will decline as the contract milestones are achieved through October 2008. As at June 30, 2008 the value of the letter of credit is \$615.

The Company's term debt consists of a term loan of US\$2,600 at June 30, 2008, bearing interest at 17.5% of the loan per annum, 12.5 % payable monthly in arrears and 5% accrued monthly but paid at the maturity, with monthly principal repayments of US\$87 commencing December 1, 2008 and continuing until maturity.

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9. OPERATING LINE OF CREDIT AND RESTRICTED CASH (continued)

The term debt liability includes the following:

	<u>June 30, 2008</u>		<u>December 31, 2007</u>	
Loan proceeds from Comvest Capital LLC	US\$	2,600	US\$	-
Financing costs		(380)		-
Common share warrants expense		(572)		-
Accretion		70		-
Term debt liability in US currency	US\$	1,718	US\$	-
Canadian Exchange		33		-
Term debt liability in Canadian currency	\$	1,751	\$	-

The Company was in breach of one of the term loan covenants at June 30, 2008 however ComVest Capital has provided a waiver. It is likely that the Company will violate covenant requirements at future compliance dates; therefore the entire balance of term debt has been classified as a current liability.

10. SHARE CAPITAL AND WARRANTS

In the three months ended June 30, 2008, the company awarded 1,298,986 options to purchase shares of the company under the stock options incentive plan.

In the three months and six months ended June 30, 2008, the Company expensed \$36 and \$72 respectively (2007 - \$60 and \$102), relating to the fair value of options granted in fiscal 2008, 2007, 2006 and 2005, as is reflected in the Consolidated Statements of Operations, Comprehensive Loss and Deficit.

In the three months ended June 30, 2008, no common share stock options were exercised, while there were 193,828 common share stock options that either expired or were cancelled.

In the three months ended June 30, 2008, the Company issued 9,300,000 common share warrants with a value of \$576, no common share warrants were exercised, and no common share warrants expired.

In the six months ended June 30, 2008, no common share stock options were exercised, while there were 289,503 common share stock options that either expired or were cancelled. As at June 30, 2008, the Company had 7,267,523 common share options outstanding.

The estimated fair value of the options is amortized to income over the vesting period, on a straight-line basis, and was determined using the Black-Scholes option pricing model with the following weighted average assumptions:

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10. SHARE CAPITAL (continued)

	2008	2007
Risk-free rate	2.7%	3.9%
Dividend yield	0%	0%
Volatility factor of expected market price of the Company's shares	96%	66%
Expected option life (in years)	4	3
Weighted-average grant date fair values of options granted	\$ 0.07	\$ 0.23

In the six months ended June 30, 2008, the Company issued 9,300,000 common share warrants with a value of \$576 which is included in share capital, no common share warrants were exercised, while there were 250,000 previously issued common share warrants with a value of \$63 that expired. As at June 30, 2008, the Company had 9,300,000 common share warrants outstanding.

The estimated fair value of the warrants was determined using the Black-Scholes pricing model with the following assumptions:

	2008	2007
Risk-free rate	2.4%	-
Dividend yield	0%	-
Volatility factor of expected market price of the Company's shares	87%	-
Expected warrant life (in years)	5	-
Fair value of warrants issued	\$ 0.06	\$ -

11. MANAGING CAPITAL

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order that it can provide future returns for shareholders and benefits for other stakeholders. Management intends to accomplish this objective with the least dilution to our shareholders and while remaining in compliance with existing or future debt covenants. The Company's current situation requires an approach to managing capital that will not generally focus on optimizing the cost of such capital and will most likely in the short-term favor debt financing.

Management believes that the use of debt to equity ratios or similar capital management tools would be inappropriate for the Company's current objectives for managing capital. Throughout 2007 and 2008 the Company did not use capital measurement tools other than those required to monitor and report on its compliance with certain debt covenants. Management is of the opinion that because these capital measurement tools are specific to certain debt instruments, and are not used on a long-term basis by Management to manage capital, disclosure of the details of their definitions and methods of calculation is inappropriate.

For the term loan secured from its bankers in the third quarter of 2007 and repaid subsequent to March 31, 2008, the Company monitored on a monthly basis its current ratio, total net worth, rolling EBITDA coverage and its annualized capital expenditures. EBITDA is defined as consolidated net income before interest, taxes, depreciation, amortization and non-cash charges and expenses other than accruals made in the normal course of business less any dividends on capital distribution.

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11. MANAGING CAPITAL (continued)

As at June 30, 2008, the Company was in breach of one debt covenant related to the ComVest term-loan. The covenant in breach was the minimum EBITDA value for the six months ended June 30, 2008. ComVest has provided a waiver. See note 9.

The Company includes shareholders' equity and all interest bearing debt in the definition of capital. The components of capital for the six months ended June 30, 2008 and the year ended December 31, 2007 are as follows:

	<u>2008</u>		<u>2007</u>
Interest bearing debt	\$ 3,790	\$	2,660
Shareholders' equity	15,363		19,355
Total Capital	\$ 19,153	\$	22,015

12. RESEARCH AND DEVELOPMENT

Research and development expenditures included in cost of revenue for the three months and six months ended June 30, 2008 were \$13 and \$36 respectively (2007 - \$33 and \$70).

13. NET LOSS PER SHARE

Basic earnings per share figures are calculated using the weighted average number of common shares outstanding during the year. Diluted earnings per share reflects the dilution that would occur if outstanding stock options and share purchase warrants were exercised or converted into common shares using the treasury stock method.

The treasury method of calculating the diluted earnings per share requires that only those of the Company's stock options and share purchase warrants whose exercise prices are lower than the average share prices for the relevant periods be used in the calculation of dilution.

The weighted average number of shares outstanding used in the calculation of basic earnings per share for the three months and six months ended June 30, 2008 was 55,993,929 and 55,993,929 respectively (2007 – 54,699,431 and 54,152,990).

The weighted average number of shares outstanding used in the calculation of the diluted earnings per share using the treasury stock method for the three months and six months ended June 30, 2008 were as follows:

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13. NET LOSS PER SHARE (continued)

	For three months ended June 30		For six months ended June 30	
	2008	2007	2007	2007
Weighted average common shares outstanding	55,993,929	54,699,431	55,993,929	54,152,990
Weighted average potential common shares	-	-	-	-
Share purchase warrants	-	-	-	-
Stock options	-	741,439	-	1,010,946
	55,993,929	55,440,870	55,993,929	55,163,936

For the three months and six months ended June 30, 2008 the inclusions of the Company's stock options and share purchase warrants in the computation of diluted loss per share had an anti-dilutive effect on earnings per share and, therefore, were excluded from the computation. Conversion of the convertible debenture in 2007 using the "if-converted" method, had an anti-dilutive effect on earnings per share and, therefore, was excluded from the computation.

14. SEGMENTED INFORMATION

	Three months ended June 30, 2008			Three months ended June 30, 2007		
	Canada	USA	Total	Canada	USA	Total
Revenue from external customers	\$ 3,835	\$ 410	\$ 4,245	\$ 15,073	\$ 168	\$ 15,241
Inter-segment revenues	\$ -	\$ 688	\$ 688	\$ -	\$ 960	\$ 960
Interest revenue	\$ 12	\$ -	\$ 12	\$ 71	\$ -	\$ 71
Interest expense	\$ 193	\$ -	\$ 193	\$ 3	\$ -	\$ 3
Amortization of capital assets	\$ 107	\$ 42	\$ 149	\$ 121	\$ 50	\$ 171
Amortization of deferred costs	\$ 373	\$ -	\$ 373	\$ -	\$ -	\$ -
Segment loss	\$ (2,128)	\$ (209)	\$ (2,337)	\$ 3,075	\$ (404)	\$ 2,671
Segment assets	\$ 23,207	\$ 592	\$ 23,799	\$ 27,784	\$ 803	\$ 28,587
Expenditures for segment capital assets	\$ -	\$ 16	\$ 16	\$ 117	\$ 75	\$ 192

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14. SEGMENTED INFORMATION (continued)

	Six months ended June 30, 2008			Six months ended June 30, 2007		
	Canada	USA	Total	Canada	USA	Total
Revenue from external customers	\$ 7,815	\$ 769	\$ 8,584	\$ 20,902	\$ 168	\$ 21,070
Inter-segment revenues	\$ -	\$ 1,280	\$ 1,280	\$ -	\$ 2,250	\$ 2,250
Interest revenue	\$ 33	\$ -	\$ 33	\$ 180	\$ -	\$ 180
Interest expense	\$ 241	\$ -	\$ 241	\$ 5	\$ -	\$ 5
Amortization of capital assets	\$ 213	\$ 91	\$ 304	\$ 235	\$ 89	\$ 324
Amortization of deferred costs	\$ 748	\$ -	\$ 748	\$ -	\$ -	\$ -
Segment loss	\$ (3,456)	\$ (1,183)	\$ (4,639)	\$ 1,609	\$ (713)	\$ 896
Segment assets	\$ 23,207	\$ 592	\$ 23,799	\$ 27,784	\$ 803	\$ 28,587
Expenditures for segment capital assets	\$ 19	\$ 17	\$ 36	\$ 234	\$ 121	\$ 355

Geographic Information

	Revenue				Capital Assets and Goodwill	
	For three months ended June 30		For six months ended June 30		June 30	
	2008	2007	2008	2007	2008	2007
Canada	\$ 2,540	\$ 13,679	\$ 4,685	\$ 17,891	\$ 12,901	\$ 13,082
International	1,705	1,562	3,899	3,179	236	394
	\$ 4,245	\$ 15,241	\$ 8,584	\$ 21,070	\$ 13,137	\$ 13,476

The allocation of revenues to the geographic segments is based upon the location of the customer.

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15. NET CHANGE IN NON-CASH WORKING CAPITAL

Net change in non-cash working capital items:

	For three months ended June 30		For six months ended June 30	
	2008	2007	2008	2007
Trade and other receivables	\$ 2,430	\$ 571	\$ 578	\$ 2,556
Unbilled revenue	142	(514)	(317)	(2,145)
Inventory	17	(43)	(6)	(100)
Accounts payable and accrued liabilities	(704)	(377)	(1,372)	(4,371)
Accrued costs on percentage completion	(10)	(380)	143	(327)
Deferred revenue	(950)	(7,289)	19	(7,400)
	\$ 925	\$ (8,032)	\$ (955)	\$ (11,787)

16. RELATED PARTY TRANSACTIONS

All related party transactions are in the normal course of operations, measured at their exchange amounts established and agreed to by the related parties. Amounts due to related parties are subject to normal trade terms. In the three months and six months ended June 30, 2008, the Company paid the following amounts to firms in which a director of the Company is an owner, partner or principal: \$75 and \$278 respectively (2007 - \$62 and \$316) for legal services. The cost of these services was charged to the ComVest term loan account as well as to general and administrative expenses. The amount due to related parties included in accounts payable and accrued liabilities as at June 30, 2008 was \$213 (2007 - \$119).