

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") explains the financial condition and results of operations of Atlantis Systems Corp. ("Company" or "we" or "our" or "us" or "ASC") as at and for the three months and nine months ended September 30, 2009 with comparisons to the three months and nine months ended September 30, 2008 and the year ended December 31, 2008, 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 nine months ended September 30, 2009 and 2008 and the audited annual consolidated financial statements, including the notes, for the year ended December 31, 2008. We prepare our consolidated financial statements in accordance with Canadian generally accepted accounting principles ("GAAP").

All amounts, with the exception of the "Highlights and Summary" section of this MD&A, are stated in thousands of Canadian dollars, except per share amounts, unless otherwise noted. All tabular amounts are expressed in thousands of Canadian dollars, except per share amounts. All non-dollar values are as stated. The definitions found in the "Glossary of Technical Terms" section of this MD&A are incorporated into this document.

This MD&A is based on information available as at November 20, 2009 except where otherwise noted.

Table of Contents

	Page
1. HIGHLIGHTS AND SUMMARY	4
2. FORWARD-LOOKING STATEMENTS.....	6
3. WHO WE ARE.....	7
4. OUR TRADITIONAL MARKETS.....	7
5. OUR TRADITIONAL TRAINING ORIENTED VALUE EQUATION	8
6. OUR STRATEGIC DIRECTION.....	9
7. OTHER COMPANY INFORMATION.....	10
8. COMVEST AGREEMENT	10
9. BRIDGE FINANCING	11
10. TSX DELISTING REVIEW	12
11. DISCONTINUED U.S. OPERATIONS	12
12. COST REDUCTION INITIATIVES.....	13
13. THE CFTS PROGRAM	15
14. RESULTS OF OPERATIONS.....	16
15. CASH FLOW , LIQUIDITY AND CAPITAL RESOURCES	27
16. LIQUIDITY.....	28
17. CAPITAL RESOURCES.....	30
18. OUTSTANDING SHARE DATA	31
19. COMMITMENTS AND CONTINGENCIES	32
20. USE OF FINANCIAL DERIVATIVES	32
21. RELATED PARTY TRANSACTIONS	32
22. SUBSEQUENT EVENTS	34
23. ACCOUNTING POLICY DEVELOPMENTS	34
24. CRITICAL ACCOUNTING ESTIMATES.....	37
25. BUSINESS OUTLOOK.....	37
26. REPORT ON DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING.....	39

GLOSSARY OF TECHNICAL TERMS ⁽¹⁾

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.

“CAE-OTSP” means the master OTSP contract, contracted between CAE and the Government of Canada

“CJ-130 FTD Program” means the flight training device program, contracted between the Company and CAE under the CAE-OTSP contract.

“CF” means Canadian Forces.

“CFTS” means contracted flying training and support.

“CPT” means cockpit procedures trainer.

“DND” means Canadian Department of National Defence.

“EBITDA” is 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.

“Eduplus” means the Eduplus division of Tecsumt Inc., acquired by ASC in the third quarter of 2007.

“GAAP” means Canadian generally accepted accounting principles.

“HVTT” means helicopter virtual task trainer.

“IMTS” means integrated maintenance training system.

“OTSP” means Operational Training Systems Provider

“MD&A” means management’s discussion & analysis

“NEX” means a separate board of the TSX Venture Exchange

Powertrain is defined as Powertrain Inc.

“PWU” means Power Workers’ Union.

“PWUTI” means Power Workers’ Union Training Inc.

“RDAF” means Royal Danish Air Force.

“SMHP” means Sikorsky Maritime Helicopter Program.

“STOC II” means the Simulation, Training and Instrumentation Omnibus Contract II as administered by the U.S. Army Program Executive Office.

“TSX” means Toronto Stock Exchange

⁽¹⁾ The definitions of the technical terms in this glossary are incorporated into the remainder of this document.

1. HIGHLIGHTS AND SUMMARY

Highlights for the Third Quarter of 2009

- During the nine months ended September 30, 2009, we have been awarded new business of approximately \$10.6 million from new contracts and from renewals and amendments to existing contracts. This new business has pushed our revenue from continuing operations for the three months ended September 30, 2009 to \$2.9 million, a 38% increase over the third quarter of 2008.
- Throughout the nine months ending September 30, 2009 we have continued to successfully implement our cost reduction initiatives for Canadian operations without impacting our ability to execute current contracts or pursue identified new opportunities. As a result, and after excluding a \$422 severance accrual in September, 2009, we have effectively decreased our operating expenses from continuing operations in the third quarter of 2009 by approximately 45% from the levels experienced in the same quarter of 2008.
- Our order backlog from continuing operations at September 30, 2009, was \$30.9 million, an increase of \$2.6 million from the same order backlog at December 31, 2008. The September 30, 2009 backlog includes \$18.9 million for CFTS program, including \$17.5 million for support services to be recognized over the next 18 years, \$4.7 million for the SMHP and \$6.5 million for three large projects awarded in 2009.
- On July 15, 2009, and August 21, 2009, CEO Capital Corporation (“CEO Capital”) provided bridge loans of \$250 and \$450, respectively, to the Company. The bridge loans are due on January 11, 2010 and August 14, 2010, unless the due dates are extended at CEO Capital’s sole option. The bridge loans were secured in order to ramp up for newly awarded contracts as well as to keep our existing programs on track. The bridge loans require interest payments of 2% per month.
- In July 2009, we reached an agreement with a U.S. based company to transfer our qualification rights to bid as a contractor with the U.S. Army under STOC II. We received an irrevocable payment of U.S. \$130 in July 2009 for completing a written submission to the U.S. Government to transfer these rights (“Novation Request”). An additional U.S. \$130 was received in October 2009 when the Novation Request was approved by the U.S. Government. Previously the Company’s board of directors (the “Board”) concluded that the future sales prospects for ASA were not sufficient to allow the U.S. subsidiary to become self-sustaining, and on this basis discontinued U.S. operations, effective June 30, 2009 (see “Discontinued Operations”).
- Our shareholders elected five new directors to the Board at the Company’s annual general and special meeting. The five individuals bring considerable business and military experience and will underscore the Company’s focus on business development going forward.

Recent Developments

On November 6, 2009, the Company accepted a proposal (the “Proposal”) from its landlord, which sets out the terms for the surrender of the existing lease and the execution of a new triple-net lease which would expire on October 31, 2014 with a stipulation that the landlord has the right to terminate the lease at any time after November 1, 2012 with nine months notice and amend the lease expiry date accordingly. Under the terms of the Proposal, the minimum rental payment under a new lease would be approximately \$24.4 per month, with annual increases of 2.0%. In addition, per the terms of the Proposal, under a new lease agreement, the Company would be obligated to pay approximately \$478 for rent in arrears prior to the expiry of the new lease; however, the landlord would also agree to release the Company from this obligation provided that the Company is not “in default” throughout the term of a new lease. The Company would also be obligated to make three equal and consecutive monthly payments, not to exceed \$350 in total, commencing on December 31, 2009 for recent repairs made by the landlord to the property. In addition, the Company would agree to complete these repairs prior to September 30, 2010. Under the terms of the Proposal, the Company would continue to be responsible for the maintenance of the property under a new lease.

Summary of the Third Quarter 2009 Results and Other Information

- Revenue from continuing operations for the three months ended September 30, 2009 was \$2.9 million, a 38% increase from revenue from continuing operations of \$2.1 million in the third quarter of the prior year. Revenues in the third quarter of 2009 and 2008 include a decrease in revenues related to prior periods due to reconfigured cost estimates to complete major programs of approximately \$0.5 million and \$0.6 million, respectively. Excluding the effect of these adjustments to revenue for both quarters, revenue for continuing operations in the third quarter of 2009 would have increased by 30% to \$3.4 million.
- Revenue from continuing operations for the nine months ended September 30, 2009 was \$8.4 million, a 16% decrease from revenue from continuing operations of \$9.9 million in the same period of the prior year. Revenue in the first nine months of 2008 also includes a decrease in revenue related to prior periods of \$2.3 million due to reconfigured cost estimates to complete major programs. In addition, the 2009 period includes a decrease in revenue of \$0.5 million, while 2008 includes an increase of \$0.25 million, from SMHP revenues due to changes in the strength of the Canadian dollar relative to the U.S. dollar. Excluding the effect of these adjustments to revenue for both periods, revenue for continuing operations in the nine-month period of 2009 would have decreased by 26% to \$8.9 million.
- Net loss from continuing operations for the three months ended September 30, 2009 was \$1.0 million, as compared to a net loss of \$2.3 million for the same period of 2008. The 2009 net loss includes a foreign exchange gain of \$0.6 million on U.S. debt.
- Net loss from continuing operations for the nine months ended September 30, 2009 was \$3.5 million, as compared to a net loss of \$6.0 million in the same period in 2008. In addition to the items affecting revenue and net income as discussed above, the net loss from continuing

operations in the first nine months of 2009 was reduced by approximately \$1.5 million for refundable tax credits and further reduced by approximately \$1.0 from a foreign exchange gain on U.S. debt. The net loss for the nine months ended September 30, 2009 also includes approximately \$0.5 million from the write-off of certain financing costs.

- Previously the Company had announced that the TSX had placed the Company under a delisting review in December 2008 as a result of a decline in the market value of the Company's common shares and concerns regarding the Company's financial condition. After considering the Company's submissions, the TSX notified the Company that its continuing listing deficiencies had not been rectified. The Company's common shares were delisted on the close of market on September 2, 2009 and began trading on the NEX, a separate board of the TSX Venture Exchange, on September 3, 2009 (NEX-AIQ.H).
- As at September 30, 2009, the Company was not in compliance with a covenant in its financing arrangement with ComVest relating to a requirement for a minimum EBITDA to Fixed Charges ratio. In addition, as at September 30, 2009, the Company had exceeded the maximum borrowing limit per the terms of its agreement with ComVest. The Company was also in arrears as at September 30, 2009 with respect to both its September 2009 principal payment and interest and fees payment. The Company chose not to request a waiver from ComVest for the September 30, 2009 reporting date in order to avoid incurring waiver fees.

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 the remainder of 2009 and for 2010 on page 37, 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. For information regarding risks and uncertainties that could affect our business, please see the Description of the Business – Risk Factors section in our Annual Information Form, and the section filed in our MD&A for the year ended December 31, 2008 contained in our 2008 Audited Financial Statements, both of which are available on the System for Electronic Data and Retrieval ("SEDAR") at www.sedar.com

It is important to note that:

- Unless otherwise indicated, forward-looking statements in this MD&A describe our expectations as of November 12, 2009.
- 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.

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. [.](#)

3. WHO WE ARE

Since our Company was founded approximately 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. In recent years, we have expanded our services into the energy sector.

In the past several years, we have also broadened our capabilities and core competencies beyond simulation and now include customized and integrated hardware and software training systems, e-learning solutions, instrumentation and control systems, and avionics test equipment.

We are headquartered in Brampton, Ontario and have an office in Halifax, Nova Scotia.

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 TRADITIONAL 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 has resulted 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 CF have an unprecedented number of major acquisition programs either underway or planned, including new airlift airframes, modernization of its 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.

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.

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.

Other Potential Markets

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

5. OUR TRADITIONAL TRAINING ORIENTED 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 operational roles; and
- to cost effectively update their training programs.

6. OUR STRATEGIC DIRECTION

In the second half of 2008, we changed our strategic focus and positioning to leverage our core competencies and existing technologies in order to broaden the value we provide to our existing customer base. We implemented strategic account management practices in order to better focus our business development and research and development activities with a view to capitalizing on additional opportunities to use simulation methods to service the full life cycle of our customers' products.

The Company is aggressively pursuing new business opportunities that align with its strategic direction.

In the third quarter of 2008, we identified the near-term priorities for the Company as follows:

- structural alignment to support the new business model;
- fill the missing elements of our resource requirements;
- restructure our sales organization to develop strategic account management;
- secure key strategic partnerships;
- increase our emphasis and investment in nuclear;
- secure targeted organic business.

Since then, we have developed a strategic plan, restructured our management team, hired a new Chief Executive Officer, discontinued our unprofitable U.S. operation, established separate business units under the leadership of a single individual with full profit and loss responsibility, have continuously implemented additional cost reduction initiatives, and have, under difficult circumstances, maintained a good banking relationship with ComVest.

We have implemented strategic account management, focusing our initial efforts on four strategic accounts. This narrow, but deep, approach to account management has already begun to show results. Since the beginning of 2009, we have secured approximately \$10.6 million in new or amended contracts, including a contract with CAE to design and manufacture a C-130J FTD as part of the Government of Canada C-130J aircrew training program, a \$2.0 million e-learning contract with L-3 Communications MAPPS Inc. (“L-3 MAPPS”) to be a subcontractor for a project with the Canadian Navy for the supply of courseware development and training for the Halifax Class Integrated Platform Management System Project, and a \$1.3 million e-learning contract with the Canadian DND.

Our continuing priorities are as follows:

- recapitalize the Company;
- further reduce our cost structure;
- aggressively seek out new business;

7. OTHER COMPANY INFORMATION

We are registered under a number of quality management programs including ISO 9001:2008, AS9100:2004, CSA-Z299.1-1985, Boeing BQMS D6-82479 and Rockwell Collins RC-9000, among others.

We operate through our wholly-owned subsidiary ASI, and through ASE, a division of ASC.

At September 30, 2009, we had a total head count of 125, of which 37 were with the ASE division in Halifax, Nova Scotia.

8. COMVEST AGREEMENT

Effective April 30, 2008, the Company entered into financing arrangements by way of a revolving credit and term loan agreement (the “ComVest Agreement”) with ComVest that provided up to U.S.\$6.6 million of financing in the form of a secured term loan (the “ComVest Term Loan”) in the amount of U.S.\$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 (the “ComVest Operating Line”) of up to U.S.\$4.0 million based on a borrowing base at a rate of interest of U.S. prime plus 2% per annum with a floor of 8%. The ComVest Term Loan matures on April 30, 2011 and the ComVest Operating Line will be available until April 30, 2010, subject to a one-year extension at the option of the Company. The arrangement also involved the Company issuing the ComVest 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 discussed further in the “Liquidity” section of this document, the Company has been for all reporting periods commencing with June 30, 2008, in breach of a certain covenant under the ComVest Agreement and for all reporting periods commencing September 30, 2008, has exceeded its maximum borrowing capacity under the ComVest Operating Line. The Company was also in arrears with respect to both its September 2009 principal payment of U.S. \$87 and interest and fees payment of U.S. \$91.

The Company chose not to request a waiver in order to avoid paying a waiver fee for both the September 30, 2009 and June 30, 2009 reporting periods. As a result of the “in default” conditions at June 30, 2009, the un-accreted balance of \$594 for the finance costs associated with obtaining the ComVest Term Loan were written-off in the second quarter of 2009. The Company had previously anticipated that it would violate covenant requirements at future compliance dates and had therefore previously presented the entire balance of the Term Loan as a current liability.

On March 25, 2009, the Board agreed to re-price the ComVest Warrants from \$0.09 to \$0.03 per share. The warrant re-pricing was in lieu of covenant waiver fees that would have been otherwise charged by ComVest for waivers for the March 31, 2009 and December 31, 2008 reporting periods. The Company had secured waivers without a fee for the applicable reporting periods prior to December 31, 2008.

Effective April 1, 2009, ComVest began charging additional default interest of 5% per annum on both the Line of Credit and the Term Loan. The floor interest rate for the Line of Credit and the monthly interest rate for the Term Debt increased to 13% per annum and 17.5% per annum, respectively, for periods that the Company is in default. The deferred interest rate of 5% per annum for the Term Debt was not increased.

9. BRIDGE FINANCING

On July 14, 2009, the Company, CEO Capital, and ComVest entered into an inter-creditor agreement, whereby the parties agreed to the following: ComVest agreed to share its collateral on the ComVest loans to the Company with bridge loans provided by CEO Capital for up to \$1,500; all parties agreed as to the priority of scheduled repayments; and CEO Capital agreed to provide ComVest with a 120 day cure period in the event of default.

A director of the Company is a principal shareholder of CEO Capital which provides consulting services to the Company, principally in the areas of corporate strategy, capital restructuring and business development. The Company and CEO Capital secured the inter-creditor agreement in order to address the Company’s additional cash requirements in order to ramp up for new business awarded in 2009 as well as to maintain our high level of service on previously awarded customer programs.

On July 15, 2009, CEO Capital provided a \$250 bridge loan to the Company, secured by a promissory note, and requiring monthly interest payments of 2% of the outstanding principal. CEO Capital has extended the due date from November 11, 2009 to January 11, 2010.

On August 21, 2009, CEO Capital provided a further bridge loan of \$450, secured by receipts

subsequent to July 31, 2009 from one of the Company's largest customer programs, and requiring monthly interest payments of 2% of the outstanding principal. CEO Capital has extended the due date from December 18, 2009 to August 14, 2010. In connection with this bridge loan, the Company issued 500,000 warrants to purchase common shares of the Company to CEO Capital (see "Capital Resources").

10. TSX DELISTING REVIEW

On December 12, 2008, the TSX placed the Company under a delisting review, pursuant to Part VII of the TSX Company Manual, as a result of a decline in the market value of the Company's shares and concerns with the Company's financial condition. After considering the Company's submissions, the TSX notified the Company that its continuing listing deficiencies had not been rectified. The Company's common shares were delisted on the close of market on September 2, 2009 and began trading on the NEX, a separate board of the TSX Venture Exchange, on September 3, 2009 (NEX-AIQ.H).

11. DISCONTINUED U.S. OPERATIONS

ASA, the Company's wholly owned U.S. subsidiary, was established in 2006 to provide a direct U.S. presence in order to better facilitate winning contracts with U.S. defense contractors and the U.S. military. However, the U.S. military market, while very large, continued to prove difficult for ASA to penetrate. We had previously disclosed, consistent with our cost reduction program and our implementation of strategic account management, that unless a sizeable U.S.-based contract was obtained that was sufficient to sustain our U.S. operations, we expected to exit this market during 2009.

During the second quarter of 2009, the Board concluded that the future sales prospects for ASA were not sufficient to allow the U.S. subsidiary to become self-sustaining. On this basis the Board set an effective date of June 30, 2009, to discontinue U.S. operations. As a result, under Canadian GAAP, the assets and liabilities of ASA have been segregated and presented separately as discontinued on the consolidated balance sheet as at September 30, 2009 and December 31, 2008. The results of operations and cash flows of ASA have been segregated and presented separately as discontinued in the consolidated statements of operations, comprehensive loss and deficit and the consolidated statements of cash flows for the three months and nine months ended September 30, 2009 and 2008.

At the time of the Board's decision, ASA had completed all external revenue generating contracts and its only current remaining revenue generating activities were on behalf of ASI. ASA had provided notice of its intention to not renew the lease on its rental premises, which expired on June 30, 2009.

ASA had previously been qualified by the U.S. Army Program Executive Office for Simulation, Training and Instrumentation as a contractor under STOC II. STOC II is an indefinite delivery/indefinite quantity contracting vehicle that was created to quickly procure the next generation of simulation and training products for use by the U.S. and coalition service members. ASA's qualification provided it with the opportunity to bid on future contracts with the U.S.

Army. In July 2009, the Company reached an agreement with a US based company to transfer our qualification rights to bid as a contractor with the US Army under STOC II. We received an irrevocable payment of U.S. \$130 in July 2009 for completing a written submission to the US Government to transfer these rights (“Novation Request”). An additional U.S. \$130 was received in October 2009 when the Novation Request was approved by the US Government.

Summarized balance sheet information for discontinued operations is as follows:

	September 30, 2009	December 31, 2008
Current assets		
Cash	\$ -	\$ 59
Trade receivables	17	72
Prepaid expenses	-	84
Current assets of discontinued operations	\$ 17	\$ 215
Capital assets, net, of discontinued operations (note 9)	\$ -	\$ 144
Current liabilities		
Accounts payable and accrued liabilities	\$ 11	\$ 133
Deferred revenue		214
Current liabilities of discontinued operations	\$ 11	\$ 347

Excluded in accounts payable for discontinued operations is \$7,250 (December 31, 2008 – \$7,565) payable to the Company.

For a further discussion on the results of discontinued operations, see “Results of Operations – Discontinued Operations”.

12. COST REDUCTION INITIATIVES

The Company initiated a cost reduction plan in the fourth quarter of 2007 in order to reduce costs and overall operating expenses by approximately 15% per year. Workforce reductions and other cost cutting measures were expected to result in annualized savings of approximately \$6.4 million. Through September 30, 2009, the cost reductions we have achieved as a result of the initial plan are consistent with the original estimates.

In the fourth quarter of 2008, we incurred additional restructuring costs of approximately \$846, net of prior year accrual reversals, which included future estimated payments of \$863 under settlement agreements with three former Canadian based executive officers of the Company. This further restructuring was expected to result in annualized cost savings of approximately

\$1.5 million in 2009.

During the first nine months of 2009 the Company has implemented additional layoffs, discontinued U.S. operations, eliminated quarterly audit reviews and reduced the cash outflow on severance payments by unilaterally reducing the payout by 50%, thereby extending the payout period to offset the reduced payout amount. Through September 30, 2009, the cost reductions we have achieved as a result of these further cost reduction initiatives are consistent with our original estimate.

In addition, in September, 2009, we accrued additional severance costs of approximately \$422, which includes the future estimated payments under settlement agreements with one former executive officer and two other senior managers of the Company. This cost reduction initiative is expected to result in additional annualized cost savings of approximately \$440 per year.

To date, cost reductions at the Canadian operations have not impacted the Company's ability to execute current contracts, or pursue identified new opportunities, as our workforce reductions have been primarily focused on non-revenue generating positions.

The Company had entered into a sale-leaseback arrangement with its landlord in 1998 with the lease to expire on November 30, 2013. On November 6, 2009, the Company accepted a proposal (the "Proposal") from its landlord, which sets out the terms for the surrender of the existing lease and the execution of a new triple-net lease which would expire on October 31, 2014 with a stipulation that the landlord has the right to terminate the lease at any time after November 1, 2012 with nine months notice and amend the lease expiry date accordingly. Under the terms of the Proposal, the minimum rental payment under a new lease would be approximately \$24.4 per month, with annual increases of 2.0%. In addition, per the terms of the Proposal, under a new lease agreement, the Company would be obligated to pay approximately \$478 for rent in arrears prior to the expiry of the new lease; however, the landlord would also agree to release the Company from this obligation provided that the Company is not "in default" throughout the term of a new lease. The Company would also be obligated to make three equal and consecutive monthly payments, not to exceed \$350 in total, commencing on December 31, 2009 for recent repairs made by the landlord to the property. In addition, the Company would agree to complete these repairs prior to September 30, 2010. Under the terms of the Proposal, the Company would continue to be responsible for the maintenance of the property under a new lease.

On July 7, 2009, the Company reached an agreement (the "Stand Still Agreement") with its landlord whereby the Company could continue to defer past due rental payments of approximately \$430 until December 31, 2009, provided that monthly payments were current through to the end of December 31, 2009 (the "Stand Still Period"). Under the Stand Still Agreement, the Company forfeited its right to the final mortgage payment, which was due December 1, 2013. However, provided that the Company continues to comply with the terms of the Standstill Agreement and the existing lease agreement, the landlord will credit the final mortgage payment of \$200 towards the rent payable for October 2013 and November 2013. The mortgage receivable of \$167 (discounted at 9%) was written off in the second quarter of 2009.

Under the Stand Still Agreement, the Company would also be obligated by December 31, 2009 to pay up to \$350 to the landlord for maintenance work completed on the property.

The Company is continuing its discussion with the landlord with respect to rent relief and the further deferral of past due amounts.

13. THE CFTS PROGRAM

Early in the second quarter of 2005, the Allied Wings consortium was awarded a \$1.77 billion contract for the CFTS program by the DND and the CF to provide the design, development, installation, operation and support for the CFTS ground-based training system in Southport, Manitoba over approximately a twenty-three year period. Atlantis is one of the five members of the Allied Wings consortium with Kelowna Flightcraft Ltd. (“Kelowna”) as the prime contractor.

Our portion of the contract, which started in 2005, is currently expected to generate approximately \$72.0 million in revenues for the production phase and a further approximately \$18.9 million (including amounts recognized to date) for the twenty-year support services phase. The expected costs to complete both the production phase and the support program are reviewed regularly by project management and finance, and as a result, the respective total estimated contract value is subject to fluctuation. During 2008, the value of the CFTS contract increased by approximately \$1.1 million due to additional work covered by contract amendments and the inflation escalation clause for the support phase of the contract. This contract value further increased during the first quarter of 2009 by approximately \$0.7 million due to the inflation escalation clause for the support phase of the contract.

The initial phase of our contribution to the CFTS program involves the provision of an integrated training solution to the consortium. We, including ASA through June 30, 2009, develop and manufacture some components of this solution “in-house”, while a significant portion were provided by subcontractors.

Throughout the third quarter of 2009, we have continued to deliver on our commitments under the CFTS program. To date we have recognized revenues of \$72.0 million, including support revenues to date, and as of September 30, 2009, we had completed approximately 98% of the initial production phase, while the full contract, including the support phase, was approximately 79% complete. The Company’s percentage-of-completion revenue-recognition policy is based on the full contract value. The unrecognized remainder on the contract of \$18.9 million includes \$17.5 million for the 20-year support phase that commenced in the fourth quarter of 2007. The remaining deliverables on the initial production phase are scheduled for completion during the first quarter of 2010. The support revenues have been combined with the initial production phase revenues for the above and for all subsequent disclosure in this document.

In the fourth quarter of 2008, our senior management team visited the Southport facilities and met with the Allied Wings management team as part of our ongoing effort to deepen relationships with our strategic accounts. During this visit it became apparent that there is a potential for a significant recurring revenue stream from the CFTS program available to Atlantis, including courseware refresh and upgrades and new flight training devices. Since then we have

identified specific areas of improvement, and we have also taken steps to establish a team to provide us with a permanent presence at the Southport facility.

14. RESULTS OF OPERATIONS

The following discussion is for the continuing operations of the Company, apart from the paragraphs that pertain explicitly to discontinued operations, thereby providing a separate discussion of the material factors influencing the continuing and discontinued operating results and financial condition of our Company, as at, and for the three months and nine months ended September 30, 2009, with comparisons to the three months and nine months ended September 30, 2008, where applicable.

Continuing operations of the Company include the operating entities ASI and ASE (a division of ASC), and corporate overheads. Discontinued operations of the Company are those of ASA.

Summary Financial Information for Continuing Operations

	For the three months ended		For the nine months ended	
	September 30		September 30	
	2009	2008	2009	2008
	\$	\$	\$	\$
Revenue from continuing operations	2,937	2,124	8,391	9,939
Gross margin from continuing operations	494	249	2,783	1,259
Gross margin percentage	17%	12%	33%	13%
Operating expenses from continuing operations ⁽¹⁾	1,342	1,674	4,275	4,923
Depreciation and amortization from continuing operations	357	479	1,072	1,440
Interest expense and financing costs from continuing operations	395	281	1,767	668
Currency exchange (gain) loss on U.S. denominated debt	(637)	156	(969)	211
Net loss from continuing operations	(963)	(2,341)	(3,529)	(5,983)
Net loss per share (basic) from continuing operations	(0.02)	(0.04)	(0.06)	(0.11)
Net loss	(844)	(2,530)	(3,890)	(7,169)
Net loss per share (basic)	(0.02)	(0.05)	(0.07)	(0.13)
Total assets at end of period for continuing operations	7,865	21,214	7,865	21,214

⁽¹⁾ Includes S&M, G&A and stock option expense

Going Concern Assumption

These consolidated financial statements have been prepared on a going concern basis which assumes that the Company will be able to meet its commitments, realize its assets and discharge its liabilities in the normal course of business.

For the nine months ended September 30, 2009 the Company incurred a net loss of \$3,890 and has a working capital deficiency of \$8,978, a deficit of \$106,270 and a shareholders' deficiency of \$7,039 as at September 30, 2009. This casts substantial doubt on the Company's ability to continue as a going concern. Continuation of the Company as a going concern is dependent upon achieving profitable operations, and/or the ability of the Company to obtain additional financing

when necessary.

In addition, On December 12, 2008, the TSX placed the Company under a delisting review, pursuant to Part VII of the TSX Company Manual, as a result of a decline in the market value of the Company's shares and concerns with the Company's financial condition. After considering the Company's submissions, the TSX notified the Company that its continuing listing deficiencies had not been rectified. The Company's common shares were subsequently delisted from the Toronto Stock Exchange at the close of market on September 2, 2009. On September 3, 2009, the Company transferred its listing to the NEX, a separate board of the TSX Venture Exchange (NEX-AIQ.H).

If the going concern assumption were not appropriate for these financial statements, adjustments would be necessary in the carrying values of assets and liabilities, the reported net loss and the balance sheet classifications used.

In the opinion of management, all adjustments considered necessary for fair presentation of the Company's financial position, results of operations and cash flows have been included. Operating results for the nine months ended September 30, 2009 are not necessarily indicative of the results to be expected for any future periods.

Continuing Operations

The components of revenue for continuing operations for the three months and nine months ended September 30, 2009 and 2008 are as follows:

	Three Months ended September 30,					
	2009		2008		Change	
	\$	%	\$	%	\$	%
CFTS	236	8%	312	15%	(76)	-24%
SMHP	948	32%	674	32%	274	41%
Other military	1,082	37%	659	31%	423	64%
Other	671	10%	479	-42%	192	40%
Total	2,937	100%	2,124	100%	813	38%

	Nine Months ended September 30,					
	2009		2008		Change	
	\$	%	\$	%	\$	%
CFTS	1,631	19%	3,989	40%	(2,358)	-59%
SMHP	2,133	25%	1,860	19%	273	15%
Other military	2,999	36%	2,425	24%	574	24%
Other	1,628	16%	1,665	4%	(37)	-2%
Total	8,391	100%	9,939	100%	(1,548)	-16%

Revenue from continuing operations for the three months ended September 30, 2009 increased

by \$813, or 38%, as compared to the same period in the prior year, primarily due to revenues recognized from new military projects awarded in 2009 and an increase in revenues generated by the SMHP. Revenues in the third quarters of 2009 and 2008 include a decrease in revenues related to prior periods due to reconfigured cost estimates to complete major programs of \$482 and \$629 million, respectively. The third quarters of 2009 and 2008 also includes an increase in revenue of \$9 and 121, respectively, from the SMHP due to fluctuations during the quarter in the value of the Canadian dollar as compared to the U.S. dollar. Excluding such effects, revenue from continuing operations would have increased in the nine months ended September 30, 2009 by 30% to \$3,410.

Revenue from continuing operations for the nine months ended September 30, 2009 was \$8,391, a 16% decrease from revenue from continuing operations of 9,939 in the same period of the prior year. Revenue in the first nine months of 2009 includes a net decrease of \$40 (2008: \$2,295) due to reconfigured cost estimates to complete programs as well as an increase in the CFTS contract value from the application in 2009 of escalation clauses to the support phase of the CFTS contract. In addition, revenue in 2009 includes a decrease of \$466 (2008: an increase of \$249) from the SMHP due to fluctuations in the value of the Canadian dollar as compared to the U.S. dollar. Excluding such effects, revenue from continuing operations would have decreased in the nine months ended September 30, 2009 by 26% to \$8,897.

In most instances the projects undertaken by the Company require many months to complete. Accordingly the Company recognizes revenue on these projects based on the percentage of costs completed for each project. Adjustments in the period to previously recognized revenues can occur as a result of a change in estimate to the total project cost resulting in a higher or lower percentage of completion. When the contract value is changed, this change in the contract value must be recognized in revenue in the current reporting period for the percentage-of-completion achieved to-date.

In the case of the CFTS program, both the production phase and the support phase are considered one project for revenue recognition purposes and revenues are recognized over the 20 year contract period. A total of \$72.0 million of revenues have been recognized to date on a total contract value of \$90.9 million. This initial production portion entered into its mature phase in the third quarter of 2007 and revenues from this program have correspondingly declined in subsequent quarters. The support services portion of the CFTS contract commenced in the fourth quarter of 2007 and has approximately \$17.5 million remaining that will be recognized over the next 18 years. We believe that our performance on the CFTS contract will lead to additional contracts with both the DND and the CF.

Revenue from the CFTS program for the three months and nine months ended September 30, 2009 includes a net decrease in revenue of \$482 (2008: \$397) and \$583 (2008: \$1,207), respectively, due to reconfigured cost estimates to complete this program and an increase in the CFTS contract value from the application of escalation clauses in 2009 to the support phase of the CFTS contract. Excluding these net effects on revenue, CFTS revenue would have increased by 1% to \$718 and decreased by 57% to \$2,214, in the three months and nine months ended September 30, 2009, respectively, as compared to the corresponding period in the prior year.

We acquired the SMHP contract with the completion of the Eduplus acquisition on September 27, 2007. ASE provides the program with training design, training documentation and courseware production. We expect revenues from this program through 2011. Our SMHP contract calls for the development of e-learning based courseware (courseware developed for use on a computer system). We substantially augmented this core competency with the Eduplus acquisition and we are committed to increasing our share in this important segment of our marketplace.

This contract with Sikorsky Aircraft Corp. (“Sikorsky”) is denominated in U.S. dollars and the contractual value has remained unchanged since the Eduplus acquisition. SMHP revenue in the third quarters of 2009 and 2008 includes an increase of \$9 and 121, respectively, while SMHP revenue in the nine-month period in 2009 includes a decrease in revenue of \$466 (2008: an increase of \$249) due to fluctuations during the applicable periods in the value of the Canadian dollar as compared to the U.S. dollar. In addition, revenue in the first nine months of 2009 includes an increase in revenue of \$543 from reconfigured cost estimates to complete this program. Excluding such effects on revenue, SMHP revenues would have increased by 70% to \$939 in the third quarter of 2009 and increased by 28% to \$2,056 in the first nine months of 2009, as compared to the corresponding periods in 2008.

Revenue from other military contracts increased by 64% to \$1,082 and 24% to \$2,999 in the three months and nine months ended September 30, 2009, respectively, as compared to the corresponding period in the prior year. Other military revenue in 2009 was primarily derived from contracts awarded in 2009, and in particular, for e-learning programs with ASE and from the C-130J FTD contract with CAE, as well as from an existing naval consulting contract and from an upgrade program for the CPT previously delivered to the RDAF for the EH-101 helicopter.

Other military revenue in both the third quarter and the nine-month period of 2008 was primarily derived from the RDAF program and the CF weapons load trainers program, which were both substantially completed in the third quarter of 2008. Revenue in both the third quarter and the nine-month period of 2008 also includes a decrease in revenue of \$232 and \$1,088, respectively, due to reconfigured cost estimates to complete the RDAF program. Excluding this effect on revenue, revenue from other military contracts would have increased by 21%, and decreased by 15%, during the three months and nine months ended September 30, 2009, respectively.

In May 2009, ASI secured a contract with CAE to design and manufacture the C-130J flight training device as part of the Government of Canada C-130J aircrew training program. ASI is part of the pan-Canadian team led by CAE which won a contract to provide systems and services for Canada’s tactical airlift, medium-to-heavy helicopter, and potentially other aircraft fleets.

E learning contracts awarded to ASE in 2009 include a \$1.3 million contract with the DND to design, develop and deliver a professional development training package for aircraft maintenance workers who are preparing to assume supervisory positions as well as from the contract with L-3 MAPPs for approximately \$2.0 million. The remaining e-learning revenues are from five smaller

projects awarded to ASE in the first quarter of 2009.

Other revenues from continuing operations in the three months and nine months ended September 30, 2009 and 2008 were derived from multiple, small and short-duration contracts, and from energy sector contracts. Revenues from customers in the energy sector decreased by 48% to \$388 during the nine months ended September 30, 2009 as compared to the corresponding period in the prior year. This decrease was primarily due to revenue recognized in 2008 from a short-term \$450 contract to provide an IMTS for use as a prototype for training technicians in power plants.

During the quarter ended September 30, 2009, we had three customers from continuing operations that represented more than 10% of total revenue, Sikorsky with 31% (2008: 23%), CAE with 18% (2008: 0%) and the CFTS with 12% (2008: 11%). As at September 30, 2009, three customers from continuing operations represented more than 10% of total combined trade receivables and unbilled revenue as follows: Sikorsky with 51% (2008: 15%); CAE with 26% (2008: 0%); and the RDAF with 10% (2008: 25%).

During the nine months ended September 30, 2009, we had three customers from continuing operations that represented more than 10% of total revenue, Sikorsky and the CF each with 24% (2008: 16% and 35%, respectively) and CAE with 10% (2008: 0%).

The order backlog for continuing operations at September 30, 2009 was \$30.9 million and includes the following: \$18.9 million from the CFTS program (with approximately \$17.5 million for future support services); \$4.7 million from the SMHP; \$6.5 million in total from three large contracts awarded in 2009; and \$0.8 million from all other contracts.

The order backlog for continuing operations increased at September 30, 2009 by \$2.6 million as compared to the same backlog at December 31, 2008 (which included \$17.4 million in future support services). The increase in backlog was the result of outpacing the decrease attributable to recognizing revenues for continuing operations of \$8.4 million with the following changes in order backlog: new contracts and contract extensions and amendments awarded in the first nine months of 2009 of approximately \$10.6 million; the gross decrease (before revenue is recognized on a percentage of completion basis) of approximately \$0.9 million in the SMHP backlog from the conversion of this U.S. dollar denominated contract to Canadian dollars; and test equipment sales as well as revenue from other small contracts of approximately \$1.3 million. Order backlog is defined as that portion of a legally binding commercial agreement that has not yet been recognized as revenue.

Gross margin from continuing operations for the quarter ended September 30, 2009 was \$494, or 17% of revenue for continuing operations, as compared to a gross margin of \$249, or 12% of revenue, for the same period in 2008. Gross margin from continuing operations for the nine months ended September 30, 2009 was \$2,783, or 33% of revenue from continuing operations, as compared to a gross margin of \$1,259, or 13% of revenue, for the same period in 2008. Both periods in 2008 have been restated to exclude foreign exchange gains/losses on U.S. dollar denominated debt.

With the exception of contributions from the RDAF program, gross margins are affected on an equal basis by the corresponding changes in program revenues from cost reconfigurations and exchange rates differences. The gross margin in the three months and nine months ended September 30, 2008 includes a net reduction of only \$195 and \$363, respectively, from the RDAF program due to reconfigured cost estimates.

In addition, the gross margin from continuing operations in the nine months ended September 30, 2009 includes a reduction in the cost of revenue of \$1,473 from the recognition of Ontario Media Development Corporation (“OMDC”) refundable tax credits, net of applicable fees, received in the first two quarters of 2009. Excluding for all periods the effect of reconfigured cost estimates, exchange rate differences and refundable tax credits, the adjusted gross margin percentages for the three months and the nine months ended September 30, 2009, would have been 28% (2008: 27%), and 20% (2008: 22%), respectively. The increased gross margin as a percentage of revenue in the third quarters of both 2009 and 2008, as compared to the nine-month periods of both years, is due to a decreased contribution, on a percentage basis, to the quarterly revenues from the intrinsically low-margin CFTS program.

We incurred G&A expenses from continuing operations of \$1,180 and \$3,347 for the three months and nine months ended September 30, 2009, respectively, a decrease of 6.7% and 9.7%, respectively, as compared to the corresponding period in 2008. The expense for both 2009 periods includes an increase in our severance accrual of \$422 with respect to future estimated payments under settlement agreements executed in September 2009 with former employees of the Company. Without giving effect to this increase in the severance accrual, G&A expenses from continuing operations for the three months and nine months ended September 30, 2009 would have decreased by 40% and 21%, respectively, as compared to the same periods in the prior year.

We incurred S&M expenses from continuing operations of \$144 and \$814 for the three months and nine months ended September 30, 2009, respectively, a decrease of 60% and 26%, respectively, as compared to the corresponding period in 2008.

The reduction in both G&A and S&M expenses reflects our ongoing cost reduction efforts, partially offset by an increase in 2009 for professional and consulting fees.

We recorded stock option expenses of \$18 (2008: \$45) and \$114 (2008: \$117) for the third quarter and the nine months ended September 30, 2009, respectively.

We expect that operating costs for the remainder of 2009 and for 2010 will decrease from the levels experienced in prior periods. .

We incurred depreciation and amortization expense for continuing operations for the third quarter of 2009 of \$357, a decrease of \$122 over the same period in 2008. Depreciation and amortization expense for continuing operations for the nine months ended September 30, 2009 was \$1,072, a decrease of \$368 over the same period in 2008. These decreases are primarily due to the amortization expense of \$108 per quarter recorded during 2008 for the HVTT deferred

development costs, which were written off in the fourth quarter of 2008.

All of our financing activities relate to continuing operations. Our interest expense and financing costs, net, increased in the third quarter of 2009 by 41% to \$395. The third quarter of 2009 net expense includes interest expense of \$323, and finance and bank charges, support fees and other costs of \$72. The 2008 third quarter interest expense and financing costs, net, includes interest expense of \$285, and finance and bank charges, support fees and other costs of \$8, offset, in part, by \$12 of interest income. The interest expense component increased in the third quarter of 2009 due to the increased amount owing on the ComVest Operating Line as well as the additional default interest of 5% per annum, effective, April 1, 2009, on both the ComVest Term Loan and Operating Line. The increase in interest expense was offset, in part, by the accretion recorded in the third quarter of 2008. The accretion resulted from the GAAP requirement to use the effective interest rate method for financial liabilities stated at amortized cost in order to recognize the expense of the original financing costs, including the initial fair value of the ComVest Warrants. No accretion was recorded in the third quarter of 2009 as a result of the write-off in the second quarter of 2009 of the un-accreted financing costs associated with obtaining the ComVest Term Loan.

Finance and bank charges for the three months ended September 30, 2009 include the fair value of the warrants issued to CEO Capital in connection the bridge financing in the third quarter of 2009 (see “Bridge Financing”).

Interest expense and financing costs, net, for the nine months ended September 30, 2009, increased by more than 160% to \$1,767 as compared to \$668 in the same period of 2008. The net expense for the nine months ended September 30, 2009, includes the write-off of \$594 for the un-accreted financing costs related to the ComVest Term Loan, interest expense of \$1,068 and finance and bank charges, support fees and other costs of \$136, offset, in part, by interest income of \$31. For the same period in 2008, interest expense and financing costs, net, includes interest expense of \$526, and finance and bank charges, support fees and other costs of \$187, offset, in part, by \$45 of interest income.

The increase of \$542 in the interest expense component in the nine months ended September 30, 2009 is primarily the result of the following: higher interest rates on the ComVest Term Loan than the old term loan; the interest not incurred on the ComVest Operating Line prior to May 5, 2008; the greater amounts borrowed in 2009 on the ComVest Operating Line; and the default interest rate increase of 5%, effective April 1, 2009, on both the ComVest Term Loan and the ComVest Operating Line.

Finance and bank charges for the nine months ended September 30, 2009 also includes the cost of the waiver provided by ComVest for the March 31, 2009, and December 31, 2008, reporting periods (see “ComVest Agreement” and “Liquidity”).

In addition, the interest income in the nine months ended September 30, 2009, was primarily due to accrued interest on the OMDC refundable tax credits.

We recorded a foreign exchange gain of \$637 and \$969 for the three months and nine months

ended September 30, 2009 as a result of restating our U.S. denominated ComVest Term Debt and Operating Line in Canadian dollars equivalents at the prevailing period-end foreign-exchange rates. During the third quarter, and the first nine months of 2009, the Canadian dollar strengthened by approximately 8% and 12%, respectively, in relation to the U.S. dollar. We recorded a foreign exchange loss of \$156 and \$211 in connection with the ComVest debt for the three months and nine months ended September 30, 2008, respectively, as a result of the decrease during these periods in the value of the Canadian dollar in relation to the U.S. dollar.

There was no income tax (recovery) expense recorded for the three months and nine months ended September 30, 2009, and 2008. 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 three months and nine months ended September 30, 2009, and 2008, was offset by utilizing an equal portion of the unrecognized operating loss carry-forwards from previous years. As at September 30, 2009, we continue to carry a full valuation allowance against our income tax assets due to the continued uncertainty surrounding their full usage. We will not be required to record income tax expense against earnings in Canada until either all unrecognized operating loss carry-forwards are utilized or expire. As of December 31, 2008, our Canadian loss carry-forwards were approximately \$14,570, of which \$192 expires in 2009, and the balance between 2010 and 2028. Furthermore, we will not be required to record income tax expense against earnings in the US until all unrecognized operating loss carry forwards are utilized or expire. With U.S. operations now discontinued, it is unlikely the Company will be able to utilize these loss carry forwards. As of December 31, 2008, our US loss carry-forwards were approximately \$8,148 and will expire between 2024 and 2028.

For the three months ended September 30, 2009, we recognized a net loss from continuing operations of \$963 or \$0.02 per share, as compared to a net loss of \$2,341, or \$0.04 per share, for the same period in 2008. The decreased loss from continuing operations of \$1,378 was primarily due to the \$793 increase in the foreign exchange gain on the ComVest debt, as well as from an increase in gross margin, primarily due to increased revenues, and from reduced operating costs.

For the nine months ended September 30, 2009, we recognized a net loss from continuing operations of \$3,529 or \$0.06 per share, as compared to a net loss of \$5,983, or \$0.11 per share, for the same period in 2008. The decrease in net loss from continuing operations of \$2,454 was primarily due to an increase in gross margin of \$1,524 (which included the recognition in 2009 of \$1,473 of refundable tax credits), a \$1,180 increase in the foreign exchange gain on the ComVest debt and from decreased operating costs and depreciation expense. The decreased net loss was offset, in part, by the increase in interest and financing costs in 2009, which included the write-off in the second quarter of 2009 of the un-accreted ComVest financing costs.

As a result of the loss recorded for continuing and discontinued operations in both the three month periods and nine-month periods ended September 30, 2009, and 2008, potentially dilutive securities become anti-dilutive, and therefore the diluted net loss per share is unchanged from the basic net loss per share.

Discontinued Operations

Summarized income statements for the ASA are as follows:

	For the three months ended		For the nine months ended	
	September 30		September 30	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
Revenue	\$ 140	\$ 865	\$ 949	\$ 1,634
Income (loss) before impairment charge	119	(189)	(311)	(1,186)
Impairment charge on capital assets	-	-	(50)	-
<u>Net loss from discontinued operations</u>	<u>\$ 119</u>	<u>\$ (189)</u>	<u>\$ (361)</u>	<u>\$ (1,186)</u>

Included in the loss from discontinued operations for both the three-month and nine-month periods ended September 30, 2009 is a long-lived asset impairment charge of \$50 as a result of recording ASA's capital assets at the lower of carrying value and fair value, less costs to sell. Interest and general corporate overhead have not been allocated to discontinued operations.

Since its incorporation in 2006, ASA has been a subcontractor to the Company on the CFTS project and as required on certain other projects. Revenue earned by ASA on the CFTS project are recorded in continuing operations as a cost of revenue and are eliminated against such revenue in our consolidated results of operations. The revenue recorded in ASA and the corresponding cost of revenue in continuing operations for the three months and nine months ended September 30, 2009 and 2008 are as follows:

	Three months ended,		Nine months ended,	
	September 30		September 30	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
<u>Revenue of ASA and cost of revenue of ASI</u>	<u>\$ -</u>	<u>\$ 117</u>	<u>\$ 279</u>	<u>\$ 1,397</u>

For the periods indicated in the above table, ASA performed services on behalf of ASI for the CFTS project only. These revenues of ASA and the corresponding cost of revenue in ASI are excluded (consolidation elimination) from the revenues and gross margin for continuing operations in the Consolidated Statements of Operations, Comprehensive Loss and Deficit. However, the actual cost to perform CFTS related activities in ASA has been included in the cost of revenue for continuing operations.

The Company recognized revenues from discontinued operations from contracts with non-related parties of \$140 (2008: \$865) and \$949 (2008: \$1,634) in the three months and nine months ended September 30, 2009, respectively. The revenues recorded in 2009 were substantially derived from one contract awarded to ASA from a large U.S. defense contractor in the first quarter of 2008 and completed during the second quarter of 2009. Revenue in 2008 was derived from this contract as well as from two other contracts with the same

contractor, both of which were completed in the second half of 2008. As of September 30, 2009, ASA had completed all of its obligations with respect to revenue generating contacts with independent parties and had no corresponding order backlog.

Summary of Quarterly Results (unaudited)

The following are the quarterly results for the Company's eight most recently completed quarters:

	2009			2008			2007	
	30-Sept \$	30-June \$	31-March \$	31-Dec \$	30-Sept \$	30-June \$	31-March \$	31-Dec \$
Revenue	2,937	1,992	3,462	2,647	2,124	3,835	3,980	5,161
Gross margin (deficit) (1)	494	(249)	2,538	1,418	249	493	517	(42)
Operating expenses(2)	1,342	1,423	1,510	2,340	1,674	1,647	1,602	2,043
Net (loss) income from continuing operations	(963)	(2,642)	76	(15,067)	(2,341)	(1,998)	(1,644)	(2,575)
Net loss	(844)	(2,935)	(111)	(16,248)	(2,530)	(2,337)	(2,302)	(3,334)
Net loss from continuing operations per share (basic and diluted)	(0.02)	(0.05)	0.00	(0.27)	(0.04)	(0.04)	(0.03)	(0.05)
Net loss per share (basic and diluted)	(0.02)	(0.05)	0.00	(0.29)	(0.05)	(0.04)	(0.04)	(0.06)
CFTS revenues	236	340	1,055	686	312	1,888	1,789	3,010
SMHP revenues	948	138	1,048	911	674	638	549	591
Non-CFTS and SMHP revenues from continuing operations	1,753	1,514	1,359	1,050	1,138	1,309	1,642	1,560

(1) Prior quarters are restated to exclude foreign exchange gains/losses on U.S. dollar denominated debt.

(2) Includes G&A, S&M and stock option expense

The Company has been dependent over each of the last eight quarters on a small number of high-dollar value contracts, and in particular, the SMHP and the CFTS program.

The initial production phase of the CFTS program entered into its mature phase in the third quarter of 2007, and as at the end of the third quarter of 2009 is approximately 98% complete. As a result, quarterly CFTS revenues have generally decreased since the third quarter of 2007. The increase recorded in the first quarter of 2009 for the CFTS program reflects a positive adjustment to revenue from reconfigured cost estimates to complete this program as well as the increases in forecasted support billings from the application of escalation clauses in the CFTS contract. CFTS revenues in the third and fourth quarters of 2008 and the second and third quarters of 2009 reflect negative adjustments to revenue from reconfigured cost estimates to complete this program.

We acquired the SMHP contract with the completion of the Eduplus acquisition on September 27, 2007 and expect revenues from this program through 2011. Revenue in the first quarter of 2009 includes an increase of \$543 from the reconfiguration of cost estimates

to complete this program. In addition, although the contractual value in U.S. dollars has remained unchanged since its acquisition, quarterly revenues have also fluctuated with the change in the relative strength of the Canadian dollar to the U.S. dollar.

The above table shows that the contributions to quarterly revenues from other than the SMHP and the CFTS program have increased beginning with the fourth quarter of 2008. The second and third quarters of 2009 include revenues of \$723 and \$823 from higher margin contracts awarded to the Company in 2009 for e-learning programs and the C-130J FTD. Revenues in the first quarter of 2009 included \$317 from the first of these e-learning contracts awarded to ASE, as well as contributions from an amended contract to provide enhancements to the CPT that was delivered under the RDAF contract. Revenues in the fourth quarter of 2008 included \$365 from the amended RDAF contract.

The Revenues from other than the CFTS and SMHP from the fourth quarter of 2007 to the third quarter of 2008 include significant contributions from the RDAF program and CF weapons load trainers program. Both programs entered the mature phase in the third quarter of 2007. In addition, revised cost estimates for the RDAF program resulted in a decrease to revenues from this program in the second and third quarters of 2008 of \$856 (gross margin: \$168) and \$232 (gross margin: \$195), respectively.

All eight quarters also included contributions from the energy sector and from numerous smaller, short-term contracts.

As the CFTS project reached maturity, the Company began to experience substantial quarterly net losses from continuing operations beginning in the third quarter of 2007. Commencing with the fourth quarter of 2007, the Company has continuously engaged in restructuring and other cost reduction initiatives in order to reduce its overhead and operating costs.

The net loss and net loss from continuing operations also reflect the effect on gross margin from changes in foreign exchange rates on the SMHP program, and changes in estimates of the cost to complete all major programs, as discussed above (also see revenue and gross margin discussions in “Results of Operations – Continuing Operations”).

The loss in the third quarter of 2009 was reduced by a foreign exchange gain of \$637 on U.S. denominated debt, and increased by the \$422 addition to our severance accrual. The loss in the second quarter of 2009 was increased by the \$594 write-off of the un-accreted financing costs related to the ComVest Term Loan, while the loss in the first quarter of 2009 was decreased by the recognition of \$1,306 of OMDC refundable tax credits, net of applicable fees.

The net losses in the fourth quarter of 2008 and 2007 increased over the other quarters presented as a result of restructuring and severance accruals for overhead and operating expenses of \$846 (including the effect of reversals in 2008 of amounts accrued in 2007) and \$802 in the fourth quarter of 2008 and 2007, respectively. Included in these amounts are \$45 and \$110 for restructuring and severance accruals in discontinued operations in the fourth

quarter of 2008 and 2007, respectively. The fourth quarter of 2008 also includes the write-off of goodwill and the HVTT deferred development costs.

During the first three quarters of 2008, the effect on quarterly losses from decreased quarterly revenues was mitigated by the cumulative effects of the initial cost reduction initiatives. During the first three quarters of 2009 the loss each quarter was further mitigated by the additional cost reduction initiatives in the fourth quarter of 2008. However, subsequent to first quarter of 2008, the effect of the continuous cost reduction initiatives has been partially offset by the increasing interest and financing costs on the ComVest Term Loan and ComVest Operating Line.

Both the quarterly net loss per share (basic) and the quarterly net loss per share (basic) for continuing operations reflect increases in the number of common shares outstanding. In September, 2007, the Company issued 1,294,498 common shares pursuant to the Eduplus acquisition. No additional common shares were issued in the last eight quarters. As at September 30, 2009, the number of outstanding common shares was 55,993,929.

For all quarters, both the diluted net loss per share and the diluted net loss per share for continuing operations did not result in any dilution versus the reported basic earnings per share.

15. CASH FLOW , LIQUIDITY AND CAPITAL RESOURCES

Summary

At September 30, 2009, we had bank indebtedness, net of cash, of \$5,373 as compared to bank indebtedness, net of cash, of \$1,370 at September 30, 2008. The sources and uses for the changes in bank indebtedness, net, for the three months and nine months ended September 30, 2009 and 2008, are as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Cash flows provided by (used in)				
Operating activities	\$ (57)	\$ (334)	\$ (2,832)	\$ (4,731)
Investing activities	-	-	(3)	(36)
Financing activities	514	-	(121)	(432)
Foreign exchange gain on US\$ Term Loan	(183)	80	(259)	109
Increase in bank indebtedness ⁽¹⁾	274	(254)	(3,215)	(5,090)
Bank indebtedness at beginning of period	(5,647)	(1,116)	(2,158)	3,720
Bank indebtedness at end of period	\$ (5,373)	\$ (1,370)	\$ (5,373)	\$ (1,370)

⁽¹⁾ For further detail of the components from continuing and discontinued operations, see Consolidated Statements of Cash Flows.

Operating Activities

For the three months ended September 30, 2009, the cash outflows from operating activities of \$57 (2008: \$334) were primarily due to a net loss from operating activities for continuing

operation of \$963 (2008: \$2,341), which was decreased by non-cash charges from continuing operations of \$385 (2008: \$648) and further decreased by an inflow of \$178 (2008: \$2,202) from the net change in non-cash working capital from continuing operations and a net inflow from discontinued operations of \$342 (2008: increased by a net outflow of \$840).

For the nine months ended September 30, 2009, the cash outflows from operating activities of \$1,318 (2008: \$4,232) were due to a net loss from continuing operations of \$3,529 (2008: \$5,983), which was decreased by non-cash charges from continuing operations of \$1,139 (2008: \$311) and increased by an outflow of \$1,059 (2008: decreased by an inflow \$1,719) from the net change in non-cash working capital from continuing operations, and further increased by a net outflow from discontinued operations of \$445 (2008: \$2,206). The \$1,059 cash outflow in 2009 from the net changes in non-cash working capital items related to continuing operations was primarily due to an increase in trade receivables and unbilled revenue, and a partially offsetting increase in accounts payable and deferred revenue.

Investing Activities

For the third quarters of 2009 and 2008, no cash was used in, or provided by, investing activities. For the nine months ended September 30, 2009 the cash used by investing activities was \$3 (2008: \$36). The nine-month period in 2009 includes a \$21 inflow from discontinued operations for the proceeds from the disposal of the capital assets of ASA. All periods reflect the expected minimum level of investment in capital assets under our cost reduction initiatives. We expect that our capital expenditures will remain at minimum levels until business levels increase, and any additions during such time will reflect specific project requirements.

Financing Activities

All financing activities relate to continuing operations. Cash inflows from financing activities for the three months ended September 30, 2009 were \$514 (2008: nil) and includes inflows of \$700 from bridge loans, net of principal payments for two months on the Term Loan. Cash outflows from financing activities for the nine months ended September 30, 2009 were \$121 (2008: 432) and also reflect the proceeds from the bridge loans, net of repayments of principal on the Term Loan. As at September 30, 2009, the September, 2009 principal payment of U.S \$87 was in arrears. The 2008 outflows reflect the repayment of the old term loan with the proceeds received May 5, 2008, from the ComVest Term Loan, and related principal repayments.

16. LIQUIDITY

Effective April 30, 2008, we entered into financing arrangements with ComVest that provided us to U.S.\$6.6 million of financing in the form of a secured term loan in the amount of U.S.\$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. In addition, the ComVest Agreement included an operating line of up to U.S. \$4.0 million based on a borrowing base at a rate of interest of U.S. prime plus 2% per annum, with a floor of 8%. The ComVest Term Loan matures on April 30,

2011 and the ComVest Operating Line will be available until April 30, 2010, subject to a one-year extension at the option of the Company. Pursuant to the ComVest Agreement, the Company issued the ComVest Warrants. (See “ComVest Agreement”).

As at September 30, 2009, we had borrowed \$5,434 (U.S. \$5,075) under the ComVest Operating Line facility. The ComVest Agreement provides for a maximum borrowing base, based on the current month trade receivables and unbilled revenue balance, and permits us to borrow funds directly for operating and subsidiary funding purposes. As at September 30, 2009, the Company had exceeded the maximum borrowing limit of the Operating Line by approximately U.S. \$2,906. The Company had also exceeded the maximum borrowing limit at June 30, 2009, March 31, 2009, December 31, 2008 and September 30, 2008 by U.S. \$3,594, U.S. \$1,398, U.S. \$2,469 and U.S. \$665, respectively.

In addition, the ComVest Agreement contains covenants for the minimum requirement of an EBITDA to Fixed Charges ratio and an annual maximum capital expenditure limit. EBITDA is defined in the ComVest Agreement 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. Fixed Charges are defined as the sum of the following: all principal payments scheduled or required to be made during the period with respect to the ComVest Loan; all related interest expense of the period; and all income taxes paid or accrued for that period.

At September 30, 2009, June 30, 2009 and March 31, 2009, the Company was not in compliance with the covenant included in the ComVest Agreement related to the rolling requirement for the previous four quarters of a minimum ratio of EBITDA to Fixed Charges of 1.25 to 1.0. The Company was also not in compliance with the EBITDA covenant at December 31, 2008 (a requirement of a minimum ratio of EBITDA to Fixed Charges of 1.1 to 1.0), September 30, 2008 (a requirement of a nine-month rolling minimum EBITDA of negative \$1.8 million) and June 30, 2008 (a requirement of a six-month rolling minimum EBITDA of negative \$2.0 million).

The Company was also in arrears with respect to both its September 2009 principal payment of US\$87 and interest and fees payment of US\$91.

The Company did not subsequently request a waiver from ComVest for the September 30, 2009 reporting date in order to avoid waiver fees.

The Company did not also request a waiver for its breach of the EBITDA covenant, or for exceeding its maximum borrowing limit for the revolving Line of Credit, at June 30, 2009, in order to avoid waiver fees. As a result of these “in default” conditions, the un-accreted balance of \$594 for the finance costs associated with obtaining the ComVest Term Loan were written-off in the second quarter of 2009. The Company had previously anticipated that it would violate covenant requirements at future compliance dates and had therefore previously presented the entire balance of the Term Loan as a current liability.

On March 25, 2009, the Board agreed to re-price, subject to regulatory approval, the ComVest Warrants from \$0.09 to \$0.03 per share. The Company received TSX approval for the re-pricing on April 9, 2009. The warrants were re-priced in lieu of covenant waiver fees that would have

been otherwise charged by ComVest for covenant waivers as of December 31, 2008 and March 31, 2009. ComVest had previously agreed to provide waivers without charge for all reporting periods prior to December 31, 2008.

Effective April 1, 2009, ComVest commenced charging additional default interest of 5% per annum on both the Line of Credit and the Term Loan. The floor interest rate for the Line of Credit and the paid-monthly interest rate for the Term Debt would be 13% per annum and 17.5% per annum, respectively, for periods that the Company is in default. The deferred interest rate of 5% per annum for the Term Debt did not change.

The Company is currently dependent on ComVest's support and the loss of ComVest's support in the near term would likely result in the Company being unable to continue operations. Any attempt by the Company to arrange financing to replace the ComVest Agreement would require the approval and interim cooperation of ComVest. The Company is currently engaged in further discussions with ComVest with respect to the nature of our relationship.

On April 15, 2009, the Company received a partial payment for OMDC refundable tax credits of approximately \$1,306, net of applicable fees, and on May 15, 2009 received the balance of \$167, net of applicable fees.

The Company's stock price on the TSX had declined substantially over the past eight quarters and its final closing price on September 2, 2009, prior to the delisting of its common shares, was \$0.02. The Company's closing price on November 20, 2009 on the NEX was \$0.015. As a result, the Company is currently dependent on its lenders, cash generated from current and new projects, and refundable investment tax credits for its liquidity.

17. CAPITAL RESOURCES

Stock Options

During the quarter ended September 30, 2009, the Company awarded 1,250,000 options to purchase common shares of the Company under our stock option plan (the "Plan"). These options were granted to five current and former directors of the Company as partial compensation for their services as directors for the period from June 12, 2008 to August 25, 2009. These options are exercisable at \$0.025 per share, have a one-year term, and vest immediately.

In addition, during the nine months ended September 30, 2009, the Company awarded an additional 1,000,000 options under the Plan. These options are exercisable at \$0.04 per share for a term of five years and fully vested within 180 days of the date of the grant.

No options were exercised during 2009, and 992,601 and 2,909,814 stock options were either cancelled or expired during the three months and nine months ended September 30, 2009, respectively.

As at September 30, 2009, 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 7,247,093 options to purchase common shares outstanding, leaving 1,151,996 options available for issuance under the Plan. The amount of options available for issuance will change as we grant options and as the actual number of common shares outstanding changes.

During the three months and nine months ended September 30, 2009, the Company recorded a net stock option compensation expense of \$18 (2008 - \$45) and \$114 (2008 - \$117), respectively, for the combination of the vesting of existing options, the grant of new options and the recognition of cancelled options. The calculation of the compensation expense includes determining the fair value of each option as calculated on the date of the grant using the Black-Scholes option pricing model.

Warrants

On March 25, 2009, the Board agreed to re-price the ComVest Warrants, subject to regulatory approval, from \$0.09 to \$0.03 per share. The expense related to re-pricing these warrants was credited to warrants within the share capital account.

On August 28, 2009, the Company issued 500,000 warrants to purchase common shares of the Company to CEO Capital, in connection with a bridge financing. The warrants have an exercise price of \$0.025 per share and expire on August 28, 2011 (See “Liquidity” and “Bridge Financing”).

In the three months and nine months ended September 30, 2009, no common share warrants were exercised or expired.

Contributed Surplus

Our contributed surplus as at September 30, 2009, increased by \$114 to \$9,314 from December 31, 2008 as a result of the stock option compensation expense recognized in the Consolidated Statement of Operations.

18. OUTSTANDING SHARE DATA

The following table summarizes the changes in the common shares, common share purchase warrants and options to purchase common shares from December 31, 2008 to October 31, 2009.

	Common Shares	Warrants	Options
Outstanding at December 31, 2008	55,993,929	9,300,000 ⁽¹⁾	7,906,907
Issued / Exercised	-	-	2,250,000
Granted	-	500,000	-
Cancelled / Expired	-	-	(3,011,814)
Outstanding at October 31, 2009	55,993,929	9,800,000	7,145,093

⁽¹⁾ See “Capital Resources – Warrants”

As at October 31, 2009, there were 9,300,000 and 500,000 common share purchase warrants outstanding at an exercise price of \$0.03 and \$0.025 per share, respectively.

As at October 31, 2009, there were 7,145,093 stock options outstanding at exercise prices ranging from \$0.02 to \$0.68 with expiry dates from January 20, 2010 through June 28, 2012.

19. COMMITMENTS AND CONTINGENCIES

Pursuant to the agreement of purchase and sale between Tecsuit and the Company, under which we purchased the Eduplus assets from Tecsuit on September 27, 2007, the two parties entered into a teaming agreement which established certain rights and obligations going forward for both parties. In addition, the Company was obligated to pay up to \$500 for future milestone based payments, on a cash neutral basis, equivalent to the gross margin on payments received by the Company for the Sikorsky Marine Helicopter Program contract that was assumed with the Eduplus acquisition.

The Company received a demand letter from Tecsuit's counsel demanding \$500 plus interest pursuant to these provisions of the teaming agreement, and has since entered into a settlement agreement which will see future payments made by Sikorsky paid into escrow until the final settlement amount, not to exceed \$450, is paid in full. The settlement agreement was executed by both parties on September 15, 2009. Under the terms of the settlement agreement, for each payment made by Sikorsky Aircraft Corporation into the escrow account, 10% of the amount was to be paid to Tecsuit, and the remainder to the Company. However, as of November 12, 2009, an amount of \$92 remains payable to Tecsuit, and represents 10% of payments received by the Company from Sikorsky subsequent to the parties reaching a verbal agreement in November 2008. An additional amount of \$28 is payable to Tecsuit pursuant to purchase price adjustments in the original agreement of purchase and sale.

20. USE OF FINANCIAL DERIVATIVES

We may use foreign exchange forward contracts to manage exposures created when sales and purchases are made in foreign currencies. As at September 30, 2009, there were no foreign exchange forward contracts outstanding (December 31, 2008 - nil).

We have not used derivative instruments to reduce our exposure to interest rate risk or to change our exposure from fixed to floating interest rates.

21. RELATED PARTY TRANSACTIONS

All related party transactions are in the normal course of operations, measured at the exchange amounts established and agreed to by the related parties. Amounts due to related parties are subject to normal trade terms for consultants and professional service providers.

The Company incurred costs of \$61 during the first quarter of 2009 for legal services provided by Gowling Henderson Lafleur LLP ("Gowlings"), a law firm in which a former director of the Company is a partner. The former director resigned from the Board effective

March 19, 2009. As at September 30, 2009, the Company had an outstanding balance payable to Gowlings of \$98, which is included in accounts payable and accrued liabilities.

The Company recorded expenses, including related costs, of \$119 (2008 - \$215) and \$312 (2008 - \$215), during the three months and nine months ended September 30, 2009, respectively, for consulting services provided by CEO Capital. A director of the Company is a principal shareholder of CEO Capital which provides consulting services, pursuant to a consulting agreement with the Company, principally in the areas of corporate strategy, capital restructuring and business development. The consulting agreement, which commenced in July 2008 for a term of one year, and has since been extended by the Board on a monthly basis, calls for a fee of \$25 per month plus expenses. An additional amount of \$44 was expensed in each of the second and third quarters of 2009 for ongoing expenses of CEO Capital. In the event that CEO Capital earns a fee on a future capital related transaction with respect to the Company, this expense would be deducted from such fees. As at September 30, 2009, the Company had an outstanding balance payable to CEO Capital of \$41, which is included in accounts payable and accrued liabilities

The Company incurred expenses of \$19 (2008 - nil) and \$47 (2008 - nil), during the three months and nine months ended September 30, 2009, respectively, for investor-relations services provided by Breakthrough Growth Corporation (“Breakthrough”). A director of the Company has a controlling interest in Breakthrough. The Company entered into a one-year investor-relations contract with Breakthrough effective February 1, 2009 for \$5 per month plus expenses. As at September 30, 2009, pursuant to the terms of the consulting agreement, the Company had prepaid the fee for services provided in October 2009.

The Company incurred expenses of \$7 (2008 - \$27) and \$13 (2008 - \$27), during the three months and nine months ended September 30, 2009, respectively, related to corporate strategy sessions facilitated by an organization in which a director of the Company has a controlling interest. As at September 30, 2009, the Company had an outstanding balance payable to this organization of \$4 which is included in accounts payable and accrued liabilities. During the second quarter of 2009 the Company paid annual fees of \$6 on behalf of the interim CEO of the Company to the Presidents of Enterprising Organizations, an organization of which a director of the Company is a principal.

In addition, in February, 2009, the Company incurred a onetime charge of \$31 for consulting services from Harborview Advisors LLC in which a former director of the Company is a principal.

All the above related party costs have been recorded to general and administrative expense.

On July 15, 2009, CEO Capital provided a \$250 bridge loan to the Company and on August 21, 2009, advanced a further \$450 in bridge financing. There were no fees charged by CEO Capital with respect to the bridge loans except for 500,000 warrants issued to CEO Capital in connection with the second bridge loan (see “Liquidity”). The fair value of these warrants was estimated as \$10 using the Black-Scholes option pricing model. In addition, interest expense related to the bridge loans was \$27 for the three months ended September 30, 2009. These expenses have been included in interest and financing costs, net, and are not otherwise reflected in this section.

During 2008, pursuant to the consulting agreement with CEO Capital, the Company granted 2,000,000 options at an exercise price of \$0.02 per share. The amortization of the fair value of these options is not otherwise reflected in this section and has been included in stock option expense for the three months and nine months ended September 30, 2009.

22. SUBSEQUENT EVENTS

On November 9, 2009, CEO Capital agreed to extend the due date from November 11, 2009 to January 11, 2010 for a bridge loan of \$250 that was previously loaned to the Company on July 15, 2009 (see “Bridge Loans”)

The Company did not request a waiver with respect to its non-compliance with certain terms of the ComVest Agreement for the reporting period ended September 30, 2009 in order to avoid the waiver fee (see “ComVest” and “Liquidity”).

Also see “Highlights and Summary – Recent Developments”.

23. ACCOUNTING POLICY DEVELOPMENTS

The Company had previously adopted and is now utilizing the recommendations in Section 3475, Disposal of Long-Lived Assets and Discontinued Operations, of the Institute of Chartered Accountants (“CICA”) Handbook which establishes revised standards for the recognition, measurement, presentation and disclosure of the disposal of long-lived assets. The Company also adopted the recommendations of Abstract 161 of the Emerging Issues Committee (“EIC”) of the CICA with respect to the allocation of interest expense and overhead to discontinued operations.

On January 1, 2009, the Company adopted the recommendations in Section 3064, Goodwill and Intangibles, of the CICA Handbook which establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The Company also adopted the amendments to CICA Handbook Section 1000, Financial Statement Concepts, which was amended to provide consistency with Section 3064. The adoption of these amendments did not have an impact on the Company’s financial results.

On January 1, 2009, the Company adopted the recommendations in Section 1400, General Standards on Financial Statement Presentation, of the CICA Handbook which has been amended to include requirements to assess and disclose an entity’s ability to continue as a going concern.

Recently issued accounting standards

IFRS Conversion Plan

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 is expected to be converged with IFRS through a combination of two methods: as current joint-convergence projects of the U.S. Financial Accounting Standards Board and the International Accounting Standards Board (“IASB”) 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. The IASB currently, and expectedly, has projects underway that should result in new pronouncements that continue to evolve IFRS.

On May 9, 2008, the Canadian Securities Administrators (“CSA”) released Staff Notice 53-320, Disclosure of Expected Changes in Accounting Policies Relating to the Changeover to International Financial Reporting Standards. The Staff Notice addresses disclosure in the MD&A for all PAEs for interim and annual periods beginning three years before the changeover to IFRS.

The following update with respect to the status of our transition to IFRS should be read in conjunction with the detailed plan in the Company’s annual MD&A for 2008. The Company had disclosed in its annual MD&A for 2008 the following events it expected to have completed or have underway by June 30, 2009:

Task	Status as of October, 2009
<ul style="list-style-type: none"> • Complete our planning to ensure sufficient internal expertise 	<ul style="list-style-type: none"> • Complete
<ul style="list-style-type: none"> • Commence senior finance training 	<ul style="list-style-type: none"> • CFO completed an IFRS course in the third quarter of 2009.
<ul style="list-style-type: none"> • Complete the identification of all relevant GAAP-dependant covenants and contracts 	<ul style="list-style-type: none"> • Rescheduled in July to be completed in the third quarter of 2009. Completion has now been deferred to the second quarter of 2010.
<ul style="list-style-type: none"> • Commence evaluation of all differences in IFRS GAAP to Canadian GAAP 	<ul style="list-style-type: none"> • Evaluation is nearly complete, with the scheduled completion previously rescheduled to November 30, 2009.
<ul style="list-style-type: none"> • Identification and assembly of the accounting policies rewrite team 	<ul style="list-style-type: none"> • Team is identified and completion has now been deferred to the second quarter of 2010. However, our evaluation to-date of GAAP differences indicates that minimal rewriting of accounting policies will be required.

The Company had disclosed in its annual MD&A for 2008 the following events it expected to

have completed or have underway by September 30, 2009:

Task	Status as of October, 2009
<ul style="list-style-type: none"> Scoping study to be completed on required information technology changes to support IFRS 	<ul style="list-style-type: none"> Completion is now deferred to the second quarter of 2010. Preliminary review indicates that minimal changes will be required.
<ul style="list-style-type: none"> Commence the identification of all material concerns with respect to the control environment and IFRS conversion and requirements 	<ul style="list-style-type: none"> Completion is now deferred to the second quarter of 2010. Preliminary review indicates that minimal changes will be required.

We have fallen behind our previously disclosed IFRS conversion schedule. Our current financial condition has placed constraints on our staff resources in finance, information technology and administration to both plan and implement the IFRS conversion. As a result, we have deferred the completion of some activities related to our IFRS conversion plan until after the completion of our fiscal 2009 audit.

Other

In January 2009, the CICA issued Handbook Section 1582, Business Combinations, which replaces the existing standards. This section establishes the standards for the accounting of business combinations, and states that all assets and liabilities of an acquired business will be recorded at fair value. Obligations for contingent considerations and contingencies will also be recorded at fair value at the acquisition date. The standard also states that acquisition related costs will be expensed as incurred and that restructuring charges will be expensed in the periods after the acquisition date. This standard is equivalent to International Financial Reporting Standards on business combinations. This standard is applied prospectively to business combinations with acquisition dates on or after April 1, 2011. Earlier adoption is permitted. The Company is currently evaluating the impact of adopting this standard on its consolidated financial statements.

In January 2009, the CICA issued Handbook Section 1602, Non-controlling Interests, which establishes standards for the accounting of non-controlling interests of a subsidiary in the preparation of consolidated financial statements subsequent to a business combination. This standard is equivalent to International Financial Reporting Standards on consolidated and separate financial statements. This standard is effective for our fiscal periods beginning April 1, 2011. Earlier adoption is permitted. The Company believes that adopting this standard will not have an impact on its consolidated financial statements.

In January 2009, the CICA issued Handbook Section 1601, Consolidated Financial Statements, which replaces the existing standards. This section establishes the standards for preparing

consolidated financial statements and is effective for our fiscal periods beginning April 1, 2011. Earlier adoption is permitted. The Company is currently evaluating the impact of adopting this standard on its consolidated financial statements.

In June 2009, the CICA amended CICA Handbook Section 3862, Financial Instruments – Disclosure, to adopt the amendments recently made to IFRS 7 Financial Instruments Disclosures. The amendments require enhanced disclosures about fair value measurements, including the relative reliability of the inputs used in those measurements, and the liquidity risk of financial instruments. The amendments apply to financial statements relating to fiscal years ending after September 30, 2009 and comparative information is not required in the first year of application. The Company is currently assessing the impact of these amendments on the financial statements and will implement the necessary additional disclosures commencing with the annual financial statements for 2009.

24. 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, intangible assets and goodwill, and the fair value of debt instruments, 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.

25. BUSINESS OUTLOOK

The following contains forward-looking statements about our business outlook for the remainder of 2009. Reference should be made to "Forward-Looking Statements" on page 6. For a description of material factors that could cause our actual results to differ materially from the forward-looking statements in the following discussion, please see the Business Risk Factors section of the MD&A for the year ended December 31, 2008 and the Description of the Business – Risk Factors section in our Annual Information Form.

Our liquidity and ability to continue operations as currently constituted will depend on the continuing support of our lenders, the timing of recognition of our current backlog and new customer orders.

Assuming adequate liquidity, our performance during the remainder of 2009 and for 2010 will be determined by the uncertain timing of the award of military training contracts, our ability to quickly leverage our strategic accounts to address their requirements for projected upgrades, enhancements and improvements to our previously installed training systems as well as their new program requirements.

Our short term profitability will also be affected by our level of order backlog now that the initial production phase of the CFTS and RDAF programs are substantially complete. The SMHP is

expected to be completed in 2011. The programs resulting from recently secured contacts with CAE, L-3 MAPPS and the DND are in the earlier stages of revenue generation.

In terms of specific results for the remainder of fiscal 2009, we expect that:

- We will continue to implement our strategic focus to broaden the value we provide to our existing customer base and develop our strategic account management approach to selling. We anticipate with this strategy that we will have greater success in landing substantial new contracts than in recent years.
- 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 opportunities related to the CFTS program with the CF and DND 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. In the fourth quarter of 2008 our senior management team visited the Southport facilities and met with the Allied Wings management team as part of our ongoing effort to deepen relationships with our strategic accounts. During this visit it became further apparent that there is a potential for a significant recurring revenue stream from the CFTS program available to Atlantis, including courseware refresh and upgrades and new flight training devices.
- Gross margins will continue to fluctuate and will depend on our future revenue levels, changes in estimates to complete large customer programs, the relative strength of the Canadian dollar to the U.S. dollar, our ability to manage non-variable overhead costs and the margin levels attainable for anticipated new business.
- Operating expenses, excluding any one time accruals for senior staff severances, will decrease further in 2009 and 2010 from the levels experienced in prior periods as a result of our 2007 cost reduction plan, and our subsequent cost reduction initiatives in 2008 and 2009.
- Interest expense and financing costs will increase over 2008 levels due to the outstanding ComVest Term Loan, the increased borrowings on the outstanding ComVest Operating Line, and the additional default interest rate of 5% on both these instruments which became effective, April 1, 2009. Capital expenditures are expected to continue to be at minimum levels and will be driven by new business and related staffing requirements.
- Cash balances are expected to generally decline for the next two quarters as additional losses are anticipated. In addition, during this period, the Company's average days-to-collect on its receivables is expected to increase due to an increased level of billing on a certain large customer program with 75 day terms. Cash availability to fund future operations will depend on the Company's ability to secure new orders, continued support from ComVest and other lenders, and our ability to secure additional capital.

- Future unanticipated outflows and out of covenant events 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 continue to increase our backlog position and demonstrate execution of our business strategy as well as the general condition of the credit markets, and may be significantly dilutive to existing shareholders. The Company's access to credit or capital could be further restricted by the current global financial crisis which has restricted credit worldwide. The Company's access could also be restricted by the September 2, 2009 delisting by the TSX of the Company's common shares with the September 3, 2009 transfer of the listing to the NEX, a separate board of the TSX Venture Exchange. Should the Company not be able to secure additional financing, it is unlikely the Company will be able to continue operations as presently constituted (see – "Results of Operations – Going Concern Assumption").

26. 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 pursuant to National Instrument 52-109. 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 September 30, 2009.

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 have concluded that the Company's internal controls for financial reporting ("ICFR") are operationally effective, although they do not expect that these internal controls will prevent all error and all fraud. The Company's CEO and CFO have based their conclusion on the operational effectiveness of its ICFR on the results of a substantial internal review and testing process completed in the first quarter of fiscal 2009. However, 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 September 30, 2009, 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. However, in order to conserve cash, the Company has eliminated quarterly audit reviews beginning with the first quarter of 2009.

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.

November 20, 2009

Interim Consolidated Financial Statements of

ATLANTIS SYSTEMS CORP.

September 30, 2009 and 2008

ATLANTIS SYSTEMS CORP.

Table of Contents

September 30, 2009 and 2008

	<u>Page</u>
Consolidated Statements of Operations, Comprehensive Loss and Deficit	1
Consolidated Balance Sheets	2
Consolidated Statements of Cash Flows	3
Notes to the Consolidated Financial Statements	4-25

ATLANTIS SYSTEMS CORP.**Consolidated Statements of Operations, Comprehensive Loss and Deficit
For the three and nine months ended September 30 2009 and 2008
(Expressed in thousands of Canadian dollars except per share amounts)
(unaudited)**

	For the three months ended September 30		For the nine months ended September 30	
	2009	2008	2009	2008
Revenue (notes 6, 7, 18 and 19)	\$ 2,937	\$ 2,124	\$ 8,391	\$ 9,939
Cost of revenue (note 6)	2,443	1,875	5,608	8,680
Gross margin	494	249	2,783	1,259
Expenses				
General and administrative	1,180	1,265	3,347	3,706
Selling and marketing	144	364	814	1,100
Stock options	18	45	114	117
	1,342	1,674	4,275	4,923
Operating income (loss) before the undernoted items	(848)	(1,425)	(1,492)	(3,664)
Depreciation and amortization	357	479	1,072	1,440
Write-off of mortgage receivable (note 8)	-	-	167	-
Interest and financing costs, net (note 11)	395	281	1,767	668
Currency exchange (gain)/loss on foreign debt	(637)	156	(969)	211
Net loss from continuing operations	(963)	(2,341)	(3,529)	(5,983)
Net income (loss) from discontinued operations (note 6)	119	(189)	(361)	(1,186)
Net loss and comprehensive loss	(844)	(2,530)	(3,890)	(7,169)
Deficit, beginning of period	(105,426)	(83,602)	(102,380)	(78,963)
Deficit, end of period	\$ (106,270)	\$ (86,132)	\$ (106,270)	\$ (86,132)
Net loss per share (note 16)				
Basic and diluted:				
Continuing operations	\$ (0.02)	\$ (0.04)	\$ (0.06)	\$ (0.11)
Discontinued operations	-	-	(0.01)	(0.02)
Net Loss	(0.02)	(0.05)	(0.07)	(0.13)
Weighted average number of shares				
Basic and diluted	55,993,929	55,993,929	55,993,929	55,993,929

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

ATLANTIS SYSTEMS CORP.
Consolidated Balance Sheets

As at September 30, 2009 and December 31, 2008
(Expressed in thousands of Canadian dollars)

	2009 (unaudited)	2008 (audited)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 61	\$ 1,041
Trade and other receivables (note 7)	2,365	503
Unbilled revenue (note 7)	2,814	1,571
Inventory	493	315
Prepaid expenses	176	242
Current assets of discontinued operations (note 6)	17	191
	5,926	3,863
Capital assets, net		
Long-term prepaid expenses	735	976
Other long-term assets	64	57
Mortgage receivable (note 8)	77	77
Deferred development costs and core technology, net (note 10)	-	164
Capital assets of discontinued operations (note 6)	1,063	1,859
	-	168
	1,939	3,301
	\$ 7,865	\$ 7,164
LIABILITIES		
Current liabilities		
Operating line of credit (note 12)	\$ 5,434	\$ 3,258
Accounts payable and accrued liabilities	4,381	3,238
Accrued costs on percentage completion	367	424
Deferred revenue	2,062	990
Bridge loans (notes 11 and 12)	700	-
Term debt (notes 11, 12, 14 and 16)	1,949	2,197
Current liabilities of discontinued operations	11	347
	14,904	10,454
SHAREHOLDERS' (DEFICIENCY) EQUITY		
Share capital and warrants (notes 13 and 14)	89,917	89,890
Contributed surplus	9,314	9,200
Deficit	(106,270)	(102,380)
	(7,039)	(3,290)
	\$ 7,865	\$ 7,164

On behalf of the Board:



Director



Director

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

ATLANTIS SYSTEMS CORP.
Consolidated Statements of Cash Flows
For the three and nine months ended September 30, 2009 and 2008
(Expressed in thousands of Canadian dollars)
(unaudited)

	For the three months ended September 30		For the nine months ended September 30	
	2009	2008	2009	2008
Cash flows provided by (used in) :				
Operating activities :				
Net loss	\$ (844)	\$ (2,530)	\$ (3,890)	\$ (7,169)
Net income (loss) from discontinued operations	119	(189)	(361)	(1,186)
Net loss from continuing operations	(963)	(2,341)	(3,529)	(5,983)
Items not affecting cash:				
Depreciation and amortization	357	479	1,072	1,440
Write-off of mortgage receivable	-	-	167	-
Stock options expensed	18	45	114	117
Accretion on term debt	-	124	238	194
Write-off of un-accreted financing costs	-	-	594	-
Financing costs related to re-pricing of common share purchase warrants	-	-	16	-
Financing costs related to issuing of common share purchase warrants	10	-	10	-
	(578)	(1,693)	(1,318)	(4,232)
Interest on mortgage receivable	-	(4)	(3)	(12)
Long-term prepaid expenses	2	1	(7)	-
Net change in non-cash working capital (note 20)	178	2,202	(1,059)	1,719
Cash provided by (used in) discontinued operations	342	(840)	(445)	(2,206)
	(57)	(334)	(2,832)	(4,731)
Investing activities :				
Investment in capital assets	-	-	(24)	(21)
Cash provided by (used in) discontinued operations	-	-	21	(15)
	-	-	(3)	(36)
Financing activities :				
Term debt repayment	-	-	-	(2,660)
Term debt proceeds	-	-	-	2,228
Bridge loan proceeds	700	-	700	-
Principal payment on term debt	(186)	-	(821)	-
	514	-	(121)	(432)
Net cash used in (provided by) foreign exchange loss on term debt	(183)	80	(259)	109
Net increase (decrease) in cash	274	(254)	(3,215)	(5,090)
(Bank indebtedness, net) cash, beginning of period - continuing operations	(5,650)	(1,156)	(2,217)	3,605
Cash, beginning of period - discontinued operations	3	40	59	115
Bank indebtedness, net, end of period	\$ (5,373)	\$ (1,370)	\$ (5,373)	\$ (1,370)
Bank indebtedness, net, end of period - continuing operations	(5,373)	(1,537)	(5,373)	(1,537)
Cash, end of period - discontinued operations	-	167	-	167
SUPPLEMENTAL INFORMATION				
Bank indebtedness, net for continuing operations is comprised of:				
Cash	\$ 61	\$ 559	\$ 61	\$ 559
Bank operating line of credit	(5,434)	(2,096)	(5,434)	(2,096)
Bank indebtedness, net for discontinued operations is comprised of:				
Cash	\$ -	\$ 167	\$ -	\$ 167
	\$ (5,373)	\$ (1,370)	\$ (5,373)	\$ (1,370)
Interest paid	\$ 324	\$ 161	\$ 831	\$ 333
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

September 30, 2009 and 2008

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

1. NATURE OF OPERATIONS

Atlantis Systems Corp. (the “Company”) continued under the laws of Canada, and since September 3, 2009 its common shares have been listed on the NEX (note 2), a separate board of the TSX Venture Exchange (NEX-AIQ.H).

During the second quarter of 2009, the board of directors of the Company (“Board”) concluded that the future opportunities for Atlantis Systems America Inc. (“ASA”) were not sufficient to allow the Company’s US subsidiary to become self-sustaining. On this basis the Board set an effective date of June 30, 2009, to discontinue US operations (note 6) and Atlantis Systems International Inc. (“ASI”) became the sole operating subsidiary of the Company. ASI is a training integrator specializing in military, commercial aviation and energy markets worldwide. ASI combines desktop and full-flight simulation, learning management systems and multimedia courseware to provide integrated training systems to the customers. ASA provided similar services in the United States. In addition, the Company has an 85% interest in Denbridge Digital Limited, which is an inactive holding company.

The assets and liabilities of ASA have been segregated and presented separately as discontinued on the consolidated balance sheets as at September 30, 2009 and September 30, 2008. The results of operations and cash flows of ASA have been segregated and presented separately as discontinued in the consolidated statements of operations, comprehensive loss and deficit and the consolidated statements of cash flows for the three months and nine months ended September 30, 2009 and 2008 (notes 3 and 6).

2. GOING CONCERN ASSUMPTION

These consolidated financial statements have been prepared on a going concern basis which assumes that the Company will be able to meet its commitments, realize its assets and discharge its liabilities in the normal course of business.

For the nine months ended September 30, 2009 the Company incurred a net loss of \$3,890 and has a working capital deficiency of \$8,978, a deficit of \$106,270 and a shareholders’ deficiency of \$7,039 as at September 30, 2009. This casts substantial doubt on the Company’s ability to continue as a going concern. Continuation of the Company as a going concern is dependent upon achieving profitable operations, and/or the ability of the Company to obtain additional financing when necessary.

In addition, On December 12, 2008, the TSX placed the Company under a delisting review, pursuant to Part VII of the TSX Company Manual, as a result of a decline in the market value of the Company’s shares and concerns with the Company’s financial condition. After considering the Company’s submissions, the TSX notified the Company that it’s continuing listing deficiencies had not been rectified. The Company’s common shares were subsequently delisted from the Toronto Stock Exchange at the close of market on September 2, 2009. On September 3, 2009, the Company transferred its listing to the NEX, a separate board of the TSX Venture Exchange (NEX-AIQ.H).

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

If the going concern assumption were not appropriate for these financial statements, adjustments would be necessary in the carrying values of assets and liabilities, the reported net loss and the balance sheet classifications used.

In the opinion of management, all adjustments considered necessary for fair presentation of the Company's financial position, results of operations and cash flows have been included. Operating results for the nine months ended September 30, 2009 are not necessarily indicative of the results to be expected for any future periods.

3. ACCOUNTING POLICY WITH RESPECT TO DISCONTINUED OPERATIONS

The Company had previously adopted the recommendations in Section 3475, Disposal of Long-Lived Assets and Discontinued Operations, of the Institute of Chartered Accountants ("CICA") Handbook which establishes revised standards for the recognition, measurement, presentation and disclosure of disposal of long-lived assets. The Company also adopted the recommendations of Abstract 161 of the Emerging Issues Committee ("EIC") of the CICA with respect to the allocation of interest expense and overhead to discontinued operations.

4. CHANGE IN ACCOUNTING POLICIES

Goodwill and Intangibles

On January 1, 2009, the Company adopted the recommendations in Section 3064, Goodwill and Intangibles, of the Institute of Chartered Accountants ("CICA") Handbook which establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The Company also adopted the amendments to CICA Handbook Section 1000, Financial Statement Concepts, which was amended to provide consistency with Section 3064. The adoption of these amendments did not have an impact on the Company's financial results.

General Standards on Financial Statement Presentation

On January 1, 2009, the Company adopted the recommendations in Section 1400, General Standards on Financial Statement Presentation, of the CICA Handbook, which has been amended to include requirements to assess and disclose an entity's ability to continue as a going concern.

5. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

International Financial Reporting Standards

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

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

Financial Instruments – Disclosures

In June 2009, the CICA amended CICA Handbook Section 3862, Financial Instruments – Disclosure, to adopt the amendments recently made to IFRS 7 Financial Instruments Disclosures. The amendments require enhanced disclosures about fair value measurements, including the relative reliability of the inputs used in those measurements, and the liquidity risk of financial instruments. The amendments apply to financial statements relating to fiscal years ending after September 30, 2009 and comparative information is not required in the first year of application. The Company is currently assessing the impact of these amendments on the financial statements and will implement the necessary additional disclosures commencing with the annual financial statements for 2009.

Business combinations

In January 2009, the CICA issued Handbook Section 1582, Business Combinations, which replaces the existing standards. This section establishes the standards for the accounting of business combinations, and states that all assets and liabilities of an acquired business will be recorded at fair value. Obligations for contingent considerations and contingencies will also be recorded at fair value at the acquisition date. The standard also states that acquisition related costs will be expensed as incurred and that restructuring charges will be expensed in the periods after the acquisition date. This standard is equivalent to International Financial Reporting Standards on business combinations. This standard is applied prospectively to business combinations with acquisition dates on or after April 1, 2011. Earlier adoption is permitted. The Company is currently evaluating the impact of adopting this standard on its consolidated financial statements.

Non-controlling interests

In January 2009, the CICA issued Handbook Section 1602, Non-controlling Interests, which establishes standards for the accounting of non-controlling interests of a subsidiary in the preparation of consolidated financial statements subsequent to a business combination. This standard is equivalent to International Financial Reporting Standards on consolidated and separate financial statements. This standard is effective for our fiscal periods beginning April 1, 2011. Earlier adoption is permitted. The Company believes that adopting this standard will have no effect on its consolidated financial statements.

Consolidated financial statements

In January 2009, the CICA issued Handbook Section 1601, Consolidated Financial Statements, which replaces the existing standards. This section establishes the standards for preparing consolidated financial statements and is effective for our fiscal periods beginning April 1, 2011. Earlier adoption is permitted. The Company is currently evaluating the impact of adopting this standard on its consolidated financial statements.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

6. DISCONTINUED OPERATIONS

During the second quarter of 2009, the Board concluded that the future opportunities for ASA were not sufficient to allow the US subsidiary to become self-sustaining. On this basis the Board set an effective date of June 30, 2009, to discontinue US operations.

At the time of the Board's decision, ASA had completed all external revenue generating contracts and its only current remaining revenue generating activities were on behalf of ASI. ASA had provided notice of its intention to not renew the lease on its rental premises, which expired on June 30, 2009.

ASA had previously been qualified by the US Army Program Executive Office as a contractor under the Simulation, Training and Instrumentation Omnibus Contract II ("STOC II"). STOC II is an indefinite delivery/indefinite quantity contracting vehicle that was created to quickly procure the next generation of simulation and training products for use by the US and coalition service members. In July 2009, the Company reached an agreement with a US based company to transfer our qualification rights to bid as a contractor with the US Army under STOC II. We received an irrevocable payment of US \$130 in July 2009 for completing a written submission to the US Government to transfer these rights ("Novation Request"). An additional US \$130 was received in October 2009 when the Novation Request was approved by the US Government.

Summarized income statements for ASA are as follows:

	For the three months ended		For the nine months ended	
	September 30		September 30	
	2009	2008	2009	2008
Revenue	\$ 140	\$ 865	\$ 949	\$ 1,634
Income (loss) before impairment charge	119	(189)	(311)	(1,186)
Impairment charge on capital assets	-	-	(50)	-
Net income (loss) from discontinued operations	\$ 119	\$ (189)	\$ (361)	\$ (1,186)

Included in the loss from discontinued operations for the nine-month period ended September 30, 2009 is a long-lived asset impairment charge of \$50 as a result of recording ASA's capital assets at the lower of carrying value and fair value, less costs to sell. The assets were subsequently sold in the second quarter of 2009 at their decreased carrying value.

Summarized balance sheet information for discontinued operations is as follows:

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

	September 30, 2009	December 31, 2008
Current assets		
Cash	\$ -	\$ 59
Trade receivables	17	72
Prepaid expenses	-	84
Current assets of discontinued operations	\$ 17	\$ 215
Capital assets, net, of discontinued operations (note 9)	\$ -	\$ 144
Current liabilities		
Accounts payable and accrued liabilities	\$ 11	\$ 133
Deferred revenue		214
Current liabilities of discontinued operations	\$ 11	\$ 347

Excluded in accounts payable of discontinued operations is \$7,250 (December 31, 2008 – \$7,565) payable to the Company.

See note 19 for segmented information with respect to discontinued operations.

7. CONCENTRATION OF CREDIT RISK

The Company has contracts with many customers. The following table summarizes distribution of the balances as at September 30, 2009, of customers from continuing operations with the largest balances in consolidated trade receivables and unbilled revenue as well as customers with the highest consolidated revenue for the three months and nine months ended September 30, 2009:

	Percentage of Consolidated Revenue				Percentage of Consolidated Trade Receivables and Unbilled Revenue	
	For three months ended September 30		For nine months ended September 30		September 30	
	2009	2008	2009	2008	2009	2008
Customer #1	31%	23%	24%	16%	51%	15%
Customer #2	18%	0%	10%	0%	26%	0%
Customer #3	1%	11%	4%	13%	10%	25%
Customer #4	12%	11%	24%	35%	1%	23%
Various other customers	38%	55%	38%	36%	12%	37%
	100%	100%	100%	100%	100%	100%

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

8. MORTGAGE RECEIVABLE

On July 7, 2009, the Company reached an agreement (the “Stand Still Agreement”) with its landlord at the Company’s Brampton, Ontario location whereby the Company could continue to defer \$430 of past due rental payments until December 31, 2009, provided that monthly payments were current for July, 2009 and through to the end of December 31, 2009 (the “Stand Still Period”).

Under the terms of the Stand Still Agreement, the Company forfeited its right to the final mortgage payment of \$200, due December 1, 2013. This mortgage, which has now been deregistered, was pursuant to a sale-leaseback arrangement that the Company entered into with its landlord in 1998. The mortgage receivable was written-off in the second quarter of 2009.

The terms of the Stand Still Agreement further provide that if the Company continues to comply with the terms of the Stand Still Agreement, as well as the existing lease agreement, the landlord will credit an amount of \$200 towards the rent payable for the final two months of the lease. The existing lease expires on November 30, 2013. In addition, the Company would also be obligated by December 31, 2009 to pay the landlord for maintenance work completed on the property.

9. CAPITAL ASSETS

Capital assets for continuing operations consist of the following:

	September 30, 2009		
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Equipment, software, furniture and fixtures	2,483	1,871	612
Leasehold improvements	636	513	123
	3,119	2,384	735

	December 31, 2008		
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Equipment, software, furniture and fixtures	\$ 2,589	\$ 1,814	\$ 775
Leasehold improvements	635	434	201
	\$ 3,224	\$ 2,248	\$ 976

There were no remaining capital assets for discontinued operations as at September 30, 2009 as the equipment, software and furniture and fixtures were sold for proceeds equal to the carrying value

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

during the period ended June 30, 2009. An asset impairment charge of \$50 was recorded prior to this sale. The leasehold improvements were fully depreciated as ASA's lease expired on June 30, 2009.

Capital assets for discontinued operations as at December 31, 2008 consist of the following:

	December 31, 2008		
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Equipment, software, furniture and fixtures	463	326	137
Leasehold improvements	16	9	7
	<u>\$ 479</u>	<u>\$ 335</u>	<u>\$ 144</u>

10. DEFERRED DEVELOPMENT COSTS AND CORE TECHNOLOGY

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

	September 30, 2009			
	Cost	Accumulated Amortization	Impairment Loss	Net Book Value
Eduplus core technology	<u>3,188</u>	<u>2,126</u>	<u>-</u>	<u>1,062</u>

	December 31, 2008			
	Cost	Accumulated Amortization	Impairment Loss	Net Book Value
Eduplus core technology	<u>3,188</u>	<u>1,329</u>	<u>-</u>	<u>1,859</u>

Eduplus core technology is software that was acquired in the purchase of the Eduplus division of Tecsalt Inc. ("Tecsult") on September 27, 2007, and is being amortized over three years. Amortization for the three months and nine months ended September 30, 2009 was \$266 (2008 - \$266) and \$797 (2008 - \$797), respectively.

11. INTEREST AND FINANCING COSTS, NET

Interest and financing costs, net for the three months and nine months ended September 30, 2009 and 2008 are as follows:

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

	For the three months ended September 30		For the nine months ended September 30	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
Interest expense ⁽¹⁾	\$ 323	\$ 285	\$ 1,068	\$ 526
Finance and bank charges ⁽²⁾	72	8	136	187
Interest income ⁽³⁾	-	(12)	(31)	(45)
	<u>395</u>	<u>281</u>	<u>1,173</u>	<u>668</u>
Write-off of un-accreted financing costs (note 12)	-	-	594	-
	<u>\$ 395</u>	<u>\$ 281</u>	<u>\$ 1,767</u>	<u>\$ 668</u>

⁽¹⁾ Includes \$nil and \$238 for the three months and nine months ended September 30, 2009, respectively, for the accretion recorded prior to the write-off of the un-accreted financing costs (note 12).

There were no material direct interest and financing costs associated with discontinued operations and interest and financing costs, net, from continuing operations have not been allocated to discontinued operations.

12. OPERATING LINE OF CREDIT, TERM LOAN, BRIDGE LOANS AND CASH

ComVest Agreement

On April 30, 2008, the Company entered into financing arrangements with ComVest that provided up to US\$6,600 of financing in the form of a secured term loan (the "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% and is collateralized by a general security agreement over all present and future personal property. 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 on May 5, 2008 and the Term Loan was used to repay, in part, 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 ("ComVest Warrants").

The Term Loan requires monthly principal repayments of US\$87 commencing December 1, 2008 and continuing until maturity.

At September 30, 2009, the Company was in breach of a certain Term Loan covenant and had exceeded its maximum borrowing limit by US\$2,906 for the revolving Line of Credit. The Company was also in arrears with respect to both its September 2009 principal payment of US\$87 and interest and fees payment of US\$91. The Company did not subsequently request a waiver from ComVest for the September 30, 2009 reporting date in order to avoid the waiver fee.

The Company did not request a waiver for the breach of the same Term Loan covenant or for the Company exceeding its maximum borrowing limit for the revolving Line of Credit on June 30, 2009. As a result of these "in default" conditions, the un-accreted balance of \$594 for the finance

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

costs associated with obtaining the ComVest Term Loan were written-off in the second quarter of 2009. The Company had previously anticipated that it would violate covenant requirements at future compliance dates and had therefore previously presented the entire balance of the Term Loan as a current liability.

On March 25, 2009, the Board agreed to re-price the ComVest Warrants from \$0.09 to \$0.03 per share in lieu of covenant waiver fees that would have been otherwise charged by ComVest for the three month periods ending March 31, 2009, and December 31, 2008 (note 14). The expense of \$16 related to re-pricing the warrants was included in interest expense and financing costs for the first quarter of 2009.

ComVest commenced charging additional default interest of 5% per annum on both the Line of Credit and the Term Loan effective April 1, 2009. The floor interest rate for the Line of Credit and the paid-monthly interest rate for the Term Debt would be 13% per annum and 17.5% per annum, respectively for periods that the Company is in default. The deferred interest rate of 5% per annum for the Term Debt has not changed.

The Term debt liability includes the following as at September 30, 2009:

Loan proceeds from Comvest	US\$	2,600
Financing costs		(380)
Common share warrants expense		(572)
Accretion		444
Principal payment		(782)
Term debt liability in US currency prior to the write-off of un-accreted financing costs	US\$	1,310
Write-off of un-accreted financing costs in second quarter of 2009		510
Term debt liability in US currency after the write-off of un-accreted financing costs	US\$	1,820
Canadian exchange on term loan balance		129
Term debt liability in Canadian currency	\$	1,949

The Company has utilized \$5,434 (US\$5,075) of the ComVest Line of Credit as of September 30, 2009 (December 31, 2008 – \$3,258 (US\$2,675)).

Bridge Loans

On July 14, 2009, the Company, CEO Capital Corporation (“CEO Capital”), and ComVest entered into an inter-creditor agreement, whereby the parties agreed to the following: ComVest agreed to share its collateral on the ComVest loans to the Company with bridge loans provided by CEO Capital for up to \$1,500; all parties agreed as to the priority of scheduled repayments; and CEO Capital agreed to provide ComVest with a 120 day cure period in the event of default. On July 15, 2009, CEO Capital, in which a director of the Company is a principal shareholder, provided a \$250 bridge loan to the Company, secured by a promissory note. The due date for the promissory note has

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

been extended by CEO Capital from November 11, 2009 to January 11, 2010, and requires monthly interest payments of 2% of the outstanding principal (note 23).

On August 21, 2009, CEO Capital provided a further bridge loan of \$450, secured by receipts subsequent to July 31, 2009 from one of the Company's customer programs. The due date for the bridge loan has been extended by CEO from December 18, 2009 to August 14, 2010 and requires monthly interest payments of 2% of the outstanding principal. In connection with this bridge loan, the Company issued 500,000 warrants to purchase common shares of the Company to CEO Capital (note 13).

13. SHARE CAPITAL

In the three months ended September 30, 2009, a total of 1,250,000 options were awarded to purchase common shares of the Company under our stock option plan (the "Plan"). These options were granted to five current and former directors of the Company as partial compensation for their services as directors for the period from June 12, 2008 to August 25, 2009. These options are exercisable at \$0.025 per share, have a one-year term, and vested immediately.

The estimated fair value of the options awarded in the three months ended September 30, 2009, 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 assumptions:

Risk-free rate	1.5%
Dividend yield	0%
Volatility factor of expected market price of the Company's shares	192%
Expected option life (in years)	1
Weighted-average grant date fair values of options granted	\$ 0.02

In addition, during the nine months ended September 30, 2009, the Company also awarded 1,000,000 options to purchase common shares of the Company under the Plan. These options are exercisable at \$0.04 per share for a term of five years and fully vested within 180 days of the date of the grant.

In the three months and nine months ended September 30, 2009, no common share stock options were exercised. In the three months and nine months ended September 30, 2009 there were 992,601 and 2,909,814, respectively, common share stock options that either expired or were cancelled. As at September 30, 2009, the Company had 7,247,093 common share options outstanding.

In the three months and nine months ended September 30, 2009, the Company expensed \$18 (2008 - \$45) and \$114 (2008 - \$117), respectively, relating to the fair value of options granted in fiscal 2009, 2008, 2007 and 2006, as reflected in the Consolidated Statements of Operations, Comprehensive Loss and Deficit.

On August 28, 2009, the Company issued to CEO Capital 500,000 warrants to purchase common shares of the Company in connection with a bridge financing. The warrants have an exercise price of \$0.025 per share and expire on August 28, 2011.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

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

Risk-free rate	1.5%
Dividend yield	0%
Volatility factor of expected market price of the Company's shares	190%
Expected warrant life (in years)	2
Fair value of warrants issued	\$ 0.02

As at September 30, 2009, the Company also had outstanding the 9,300,000 ComVest Warrants at an exercise price of \$0.03 per share. The Board agreed on March 25, 2009 to re-price these warrants from \$0.09 per share to \$0.03 per share (notes 12 and 14). In the three months and nine months ended September 30, 2009, no common share warrants were exercised or expired.

14. 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. The Company's current situation requires an approach to managing our capital that focuses on generating sufficient cash to fund operations rather than optimizing the cost of capital.

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. During 2009 and throughout 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 and Line of Credit secured from its bankers in the second quarter of 2008 the Company monitors on a monthly basis its EBITDA to Fixed Charges ratio 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. Fixed Charges are defined as the sum of the following: all principal payments scheduled or required to be made with respect to the ComVest Tem Loan; all related interest expense; and all income taxes paid or accrued.

The Company has been in breach of the Term Loan covenant for minimum EBITDA requirements for all quarter end reporting dates commencing with June 30, 2008. In addition, the Company has exceeded its maximum borrowing limit for the revolving Line of Credit for all quarter end reporting dates beginning with September 30, 2008. The Company did not request a waiver for the September 30, 2009 and the June 30, 2009 reporting dates in order to avoid waiver fees and agreed to reprice the ComVest Warrants from \$0.09 to \$0.03 per share in lieu of covenant waiver fees that would have been otherwise charged for covenant waivers as of March 31, 2009, and December 31, 2008. ComVest had provided waivers without a fee for all breaches prior to December 31, 2008.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

During the three months ended September 30, 2009, the Company, CEO Capital, and ComVest entered into an inter-creditor agreement in order to facilitate up to \$1,500 of bridge loan financing by CEO Capital. As at September 30, 2009, the Company has received \$700 in bridge loan financing from CEO Capital, which bears interest at 2% per month. The bridge loans have enabled the Company to continue to meet its milestone delivery dates for certain large customer programs, as well as to ramp up for recently awarded contracts, and were secured without fees except for the issuance to CEO Capital of 500,000 warrants to purchase common shares of the Company (note 13).

The Company includes shareholders' (deficiency) equity and all interest bearing debt in the definition of capital. The components of capital as at September 30, 2009 and December 31, 2008 are as follows:

	<u>September 30, 2009</u>	<u>December 31. 2008</u>
Interest bearing debt	\$ 8,083	\$ 5,455
Shareholders' (deficiency) equity	(7,039)	(3,290)
Total capital	<u>\$ 1,044</u>	<u>\$ 2,165</u>

15. REFUNDABLE DIGITAL MEDIA TAX CREDITS

In the second quarter of 2009 the Company received payments in total of \$1,473, net of applicable fees, from a Government of Ontario refundable tax credit program. The Company has recorded a corresponding reduction in the cost of revenue for the nine months ended September 30, 2009.

16. 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, share purchase warrants and convertible debentures 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 and convertible debentures 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 both basic and diluted earnings per share for both the three months and nine months ended September 30, 2009 and September 30, 2008 was 55,993,929.

For the three months and nine months ended September 30, 2009 and 2008, the inclusion 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.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

17. FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Financial assets held-for-trading

Cash is classified as a held-for-trading asset and is recorded at fair value. The fair value of cash is adjusted to its fair market value at the end of each reporting period.

Financial assets recorded at amortized cost

Trade receivables and unbilled revenue are classified as loans and receivables and are recorded at amortized cost. The Company has determined that the carrying value represents fair value as at September 30, 2009. The mortgage receivable was recorded at amortized cost prior to June 30, 2009.

Financial liabilities recorded at amortized cost

All accounts payable and accrued liabilities, accrued costs on percentage completion, deferred revenue and the term debt are recorded at their amortized cost. The Company has determined that the carrying value represents fair value as at September 30, 2009.

18. FINANCIAL RISK MANAGEMENT

Overview

The Company has exposure to the following risks from its use of financial instruments:

- (a) Credit risk
- (b) Liquidity risk
- (c) Market risk

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits.

Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities.

- (a) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its obligations. The carrying amount of the Company's financial assets represents its maximum credit exposure.

Cash and cash equivalents

The Company's cash balance is on deposit in an operating account with a major Canadian bank. As at September 30, 2009, the Company had no cash equivalents. However, in accordance with its investment policy, the Company will only invest in money market

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

deposits with major Canadian Banks and with a maturity of less than 90 days. Accordingly, the Company believes it has minimal credit risk with respect to cash and cash equivalents.

Trade receivables

In the last three years, the Company's end customers have primarily been the Canadian, US, and Danish military as well as large, well-capitalized aerospace companies. When the Company does not act as the prime contractor with government agencies, the prime contractor has always been a large aerospace company. The Company has more recently contracted with large and well capitalized organizations in the Canadian energy sector. In addition to the intrinsic credit worthiness of this customer base, the Company has contracted with Export Development Canada, when risks warrant, for line of credit guarantees on certain non-domestic projects.

Historically, the Company has not experienced any significant credit losses. The Company does not have any material trade receivable balances greater than 90 days outstanding and has never recorded a material expense associated with a credit risk exposure. As a result, the Company believes that its trade receivables represent a low credit risk. However, due to the nature of the contracts and the complexity of the deliverables to its customers, the Company is exposed to a significantly greater degree of related performance risk.

(b) Liquidity risk

Liquidity risk arises through an excess of financial obligations over financial assets at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient readily available cash to meet its financial obligations as they fall due. In order to meet its financial liabilities, the Company has recently relied on collecting its trade and other receivables, utilizing its operating line of credit, and proceeds from bridge loans. In addition, the Company received payments in total of \$1,473, net of applicable fees, in Government of Ontario refundable tax credits in the second quarter of 2009.

The following are the contractual maturities of financial liabilities, including interest payments, as at September 30, 2009:

	Carrying amount	Contractual cash flows	3 months or less	3-12 months	1 - 2 years	2 - 3 years
Accounts payable and accrued liabilities from continuing operations ⁽¹⁾	\$ 4,381	\$ (4,381)	\$ (3,602)	\$ (444)	\$ (276)	\$ (59)
Accounts payable and accrued liabilities from discontinued operations	11	(11)	(11)			
Operating line of credit ⁽²⁾⁽³⁾⁽⁵⁾	5,434	(6,231)	(109)	(326)	(5,796)	
Bridge loans	700	(730)	(730)			
Term debt and deferred interest ⁽³⁾⁽⁴⁾⁽⁵⁾	2,128	(2,289)	(331)	(940)	(1,018)	
Totals - ComVest interest rates - not in default	\$ 12,654	\$ (13,642)	\$ (4,783)	\$ (1,710)	\$ (7,090)	\$ (59)
Incremental interest on term debt and line of credit for default conditions ⁽⁶⁾		(504)	(89)	(246)	(169)	-
Totals - ComVest interest rates - in default	\$ 12,654	\$ (14,146)	\$ (4,872)	\$ (1,956)	\$ (7,260)	\$ (59)

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

- (1) Does not reflect the 50% reduction of bimonthly payouts under settlement agreements with certain former executive officers. This action was taken by the Company, effective March 13, 2009, in order to conserve cash, and is expected to remain in effect until such time as cash flows permit a return to the terms of the settlement agreements. The total obligations under these agreements remain unchanged.
- (2) Assumes a non-default scenario with respect to interest rates (floor interest rate of 8% per annum). Also assumes that the operating line balance will not change from the September 30, 2009 levels (no accelerated repayment of amounts currently in excess of the borrowing limit) and that the Company will be able to exercise its option to extend the facility for one year.
- (3) Assumes September 30, 2009 US dollar exchange rate for future cash flows.
- (4) Assumes a non-default scenario with respect to interest rates (an interest rate of 12.5% per annum, paid monthly, and a deferred interest rate of 5% per annum, payable at maturity).
- (5) Assumes there is not an early repayment requirement with respect to the loan covenant or other conditions in breach.
- (6) Assumes the additional default interest rate of 5% per annum for the term loan and the line of credit, respectively, remain in effect to maturity.

The above table does not reflect future monthly commitments for lease payments and related maintenance payments for the Company's rented premises in Brampton, Ontario and Halifax, Nova Scotia (note 23).

(c) Market risk

Market risk is the risk that changes in the market prices, such as fluctuations in foreign exchange rates and interest rates, will affect the Company's net earnings or the value of its financial instruments.

Currency risk

The Company operates internationally giving rise to exposure to changes in foreign exchange rates. The currency risk is derived from revenues denominated in currencies other than the Canadian dollar, its functional currency, primarily the US dollar, and expenses associated with its US operations, as well as the respective receivable and payable balances. The Company is also exposed to currency risk on cash, other current assets and the Line of Credit and Term Loan denominated in US dollars.

Interest rate risk

The Company is exposed to interest rate risk principally on its operating Line of Credit. Under the agreement with ComVest, interest is payable throughout the term of the facility at US prime plus 2% per annum, with a floor of 8% per annum when not in default, and 13% per annum for periods when the Company is in default (note 12). The US Federal Reserve Board continuously lowered its prime lending rate throughout 2008 in response to the current global financial crisis and at September 30, 2009, the US prime interest rate was 3.25%. As a result, the Company believes it is unlikely during the next 12 months that the interest rate on this facility will exceed either floor rate and therefore expects the interest expense on the operating line to be at \$10.8 per month for each \$1,000 of operating line debt, when in default, and \$6.7

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

per month for each \$1,000 of operating line debt, should the Company not be in default. Under the agreement with ComVest, the Term Loan has a fixed monthly interest rate throughout its term of 12.5% per annum, when the Company is not in default, and when in default, an additional 5% per annum. The Company will therefore have for the remainder of the term, average monthly cash interest payments on the Term Debt of approximately \$12.6, when in default, and \$9.0 should the Company not be in default. Cash balances are deposited in highly-accessible and low-interest bank accounts and are used for short-term working capital requirements. Accordingly, the Company does not feel that an interest rate sensitivity calculation is material. However, the liquidity risk table in this note includes cash payments for interest on the Line of Credit and the Term Debt for both the in default and not in default scenarios.

Quantification of foreign currency risk

At September 30, 2009, the Company's gross balance sheet exposure to foreign currency risk for continuing operations was substantially as follows:

<i>In Canadian equivalents(000's)</i>	Canadian	US	Total
Cash	1	60	61
Trade and other receivables	2,013	352	2,365
Operating line of credit	-	(5,434)	(5,434)
Accounts payable and accrued liabilities	(3,963)	(429)	(4,392)
Bridge loan	(700)	-	(700)
Term debt		(1,949)	(1,949)
Net balance sheet exposure	(2,649)	(7,400)	(10,049)

The Company's revenue exposure, cost of revenue and operating expense exposure, and interest exposure for revenue and expenses denominated in foreign currencies for the three months and nine months ended September 30, 2009 and 2008 for continuing operations were substantially as follows:

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

Atlantis Systems Corp.						
Consolidated Revenue and Expenses Exposure to Foreign Currency Risk						
	Three months ended September 30, 2009			Nine months ended September 30, 2009		
<i>In Canadian \$ equivalents (000's)</i>	Canadian	US	Total	Canadian	US	Total
Revenue	\$ 1,718	\$ 1,359	\$ 3,077	\$ 4,790	\$ 4,550	\$ 9,340
Cost of goods sold and operating expenses	\$ 3,650	\$ 156	\$ 3,806	\$ 9,676	\$ 1,404	\$ 11,080
Interest and financing costs	\$ 5	\$ 390	\$ 395	\$ (19)	\$ 1,786	\$ 1,767
	Three months ended September 30, 2008			Nine months ended September 30, 2008		
<i>In Canadian \$ equivalents (000's)</i>	Canadian	US	Total	Canadian	US	Total
Revenue	\$ 714	\$ 2,275	\$ 2,989	\$ 5,399	\$ 6,174	\$ 11,573
Cost of goods sold and operating expenses	\$ 3,224	\$ 1,341	\$ 4,565	\$ 11,639	\$ 4,655	\$ 16,294
Interest and financing costs	\$ (11)	\$ 292	\$ 281	\$ (33)	\$ 701	\$ 668

Fair value sensitivity analysis

Gross Balance Sheet Exposure: A 10% strengthening of the Canadian dollar against the US dollar at September 30, 2009 would have decreased the net loss for continuing operations by approximately \$740 for the three month and six month periods ended September 30, 2009, respectively. This analysis assumes that all other variables, in particular interest rates, remain constant and represents the Company's gross balance sheet exposure at September 30, 2009. A 10% weakening of the Canadian dollar against the same would have had an equal but opposite effect.

Revenue Exposure: A 10% strengthening on average of the Canadian dollar against the US dollar for the three months and nine months ended September 30, 2009 would have decreased net revenue for continuing operations by approximately \$140 and \$460 for the same periods, respectively. This analysis assumes that all other variables, in particular interest rates, remained constant during the quarter, and represents the exposure of the Company's revenues denominated in foreign currencies, to the relative strength of its functional currency. A 10% weakening of the Canadian dollar against the same would have had an equal but opposite effect.

Expense Exposure: A 10% strengthening on average of the Canadian dollar against the US dollar for the three months and nine months ended September 30, 2009 would have decreased cost of goods sold, operating expenses and interest expense, in total, for continuing operations, by approximately \$55 and \$320 for the same periods, respectively. This analysis assumes that all other variables remained constant during the quarter, in particularly interest rates, and

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

represents the exposure of the Company's expenses denominated in foreign currencies, to the relative strength of its functional currency. A 10% weakening of the Canadian dollar against the same would have had an equal but opposite effect.

19. SEGMENTED INFORMATION

	Three months ended September 30, 2009			Three months ended September 30, 2008		
	Canada	USA	Total	Canada	USA	Total
Revenue from external customers	\$ 2,937	\$ 140	\$ 3,077	\$ 2,124	\$ 865	\$ 2,989
Inter-segment revenues	\$ -	\$ -	\$ -	\$ -	\$ 117	\$ 117
Interest revenue	\$ -	\$ -	\$ -	\$ 12	\$ -	\$ 12
Interest expense	\$ 395	\$ -	\$ 395	\$ 285	\$ -	\$ 285
Amortization of capital assets	\$ 91	\$ -	\$ 91	\$ 105	\$ 38	\$ 143
Amortization of deferred costs	\$ 266	\$ -	\$ 266	\$ 374	\$ -	\$ 374
Segment loss (income)	\$ (963)	\$ 119	\$ (844)	\$ (2,341)	\$ (189)	\$ (2,530)
Segment assets	\$ 7,848	\$ 17	\$ 7,865	\$ 20,057	\$ 1,157	\$ 21,214
Expenditures for segment capital assets	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

	Nine months ended September 30, 2009			Nine months ended September 30, 2008		
	Canada	USA	Total	Canada	USA	Total
Revenue from external customers	\$ 8,391	\$ 949	\$ 9,340	\$ 9,939	\$ 1,634	\$ 11,573
Inter-segment revenues	\$ -	\$ 279	\$ 279	\$ -	\$ 1,397	\$ 1,397
Interest revenue	\$ 31	\$ -	\$ 31	\$ 45	\$ -	\$ 45
Interest expense	\$ 1,204	\$ -	\$ 1,204	\$ 526	\$ -	\$ 526
Write-off of unaccreted finance costs	\$ 594	\$ -	\$ 594	\$ -	\$ -	\$ -
Amortization of capital assets	\$ 275	\$ 63	\$ 338	\$ 318	\$ 129	\$ 447
Amortization of deferred costs	\$ 797	\$ -	\$ 797	\$ 1,122	\$ -	\$ 1,122
Segment loss	\$ (3,529)	\$ (361)	\$ (3,890)	\$ (5,983)	\$ (1,186)	\$ (7,169)
Segment assets	\$ 7,848	\$ 17	\$ 7,865	\$ 20,057	\$ 1,157	\$ 21,214
Expenditures for segment capital assets	\$ 24	\$ -	\$ 24	\$ 19	\$ 17	\$ 36

The allocation of revenue in the above table is based on the location of the operational unit of the Company that performs or subcontracts the work. The US operational unit represents the discontinued operations of the Company.

Geographic Information

	Revenue				Capital Assets and Goodwill	
	For three months ended September 30		For nine months ended September 30		September 30	
	2009	2008	2009	2008	2009	2008
Canada	\$ 1,718	\$ 714	\$ 4,790	\$ 5,399	\$ 1,798	\$ 16,069
International	1,359	2,275	4,550	6,174	-	197
	\$ 3,077	\$ 2,989	\$ 9,340	\$ 11,573	\$ 1,798	\$ 16,266

The allocation of revenues in the above table to the geographic segments is based upon the location of the customer. Included in international revenue are revenues from discontinued operations of \$140 (2008 – \$865) and \$949 (2008 – \$1,634) for the three months and nine months ended September 30, 2009, respectively.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements September 30, 2009 and 2008

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

20. NET CHANGE IN NON-CASH WORKING CAPITAL

Net change in non-cash working capital of continuing operations for the three months ended September 30, 2009 and 2008:

	For three months ended September 30		For nine months ended September 30	
	2009	2008	2009	2008
Trade receivables	\$ (753)	\$ 1,324	\$ (1,862)	\$ 2,149
Unbilled revenue	(398)	973	(1,243)	656
Inventory	(50)	53	(178)	47
Prepays	35	-	66	-
Accounts payable and accrued liabilities	695	80	1,143	(1,105)
Accrued costs on percentage completion	(140)	2	(57)	171
Deferred revenue	789	(230)	1,072	(199)
	<u>\$ 178</u>	<u>\$ 2,202</u>	<u>\$ (1,059)</u>	<u>\$ 1,719</u>

21. RELATED PARTY TRANSACTIONS

All related party transactions are in the normal course of operations, measured at the exchange amounts as established and agreed to by the related parties. Amounts due to related parties are subject to normal trade terms for consultants and professional services. In the three months and nine months ended September 30, 2009, the Company incurred expenses of \$144 (2008- \$267) and \$470 (2008 - \$545), respectively, for legal services and consulting services with firms in which a director of the Company was an owner, partner or principal.

Included in accounts payable and accrued liabilities as at September 30, 2009 was \$98 due to the law firm of Gowling Henderson Lafleur LLP of which a former director of the Company is a partner. This director resigned from the Board effective March 19, 2009. The amount includes \$61 for services provided prior to the director's resignation. An additional amount of \$45 is due to related parties at September 30, 2009 and included in accounts payable and accrued liabilities.

The Company has entered into a consulting agreement with CEO Capital Corporation in which a director of the Company is a principal shareholder. The consulting agreement commenced in July 2008 for a term of one year and called for a fee of \$25 per month plus expenses. The Board has agreed to extend the consulting agreement on a monthly basis at the same fee per month. As at September 30, 2009, pursuant to the terms of the consulting agreement, the Company had prepaid the fee for services provided in October, 2009. In addition, an amount of \$44 for ongoing expenses of CEO Capital was paid and expensed in both the second and third quarters of 2009. These expenses will be deducted from any fees due to CEO Capital in the event the consultant earns a fee with respect to future capital related transaction of the Company.

Effective February 1, 2009, the Company has entered into a one-year investor-relations contract with Breakthrough Growth Corporation in which a director of the Company has a controlling interest. The agreement calls for a fee of \$5 per month plus expenses. As at September 30, 2009, pursuant to the terms of the consulting agreement, the Company had prepaid the fee for services provided in October, 2009.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

The Company also incurred expenses during the three months and nine months ended September 30, 2009 related to corporate strategy sessions of \$7 and \$13, respectively, to an organization in which a director of the Company has a controlling interest. During the nine months ended September 30, 2009, the Company paid annual fees of \$6 to the Presidents of Enterprising Organizations, an organization of which a director of the Company is a principal, on behalf of the interim CEO of the Company.

In February, 2009, the Company incurred a onetime charge of \$31 for consulting services from Harborview Advisors LLC (“Harborview”), at which time a principal of Harborview was a director of the Company.

All the above related party expenses have been included in general and administrative expense.

On July 15, 2009, CEO Capital provided a \$250 bridge loan to the Company and on August 21, 2009, advanced a further \$450 in bridge financing. There were no fees charged by CEO Capital with respect to the bridge loans except for 500,000 warrants issued to CEO Capital in connection with the second bridge loan (note 12). The fair value of these warrants was estimated as \$10 using the Black-Scholes option pricing model. In addition, interest expense on the bridge loans was \$27 for the three months ended September 30, 2009. These expenses are included in interest and financing costs, net, and are not otherwise reflected in this note.

22. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted for the current quarter.

23. SUBSEQUENT EVENTS

On November 9, 2009, CEO Capital agreed to extend the due date from November 11, 2009 to January 11, 2010 for a bridge loan of \$250 that was previously loaned to the Company on July 15, 2009 (note 12).

On November 6, 2009, the Company accepted a proposal (the “Proposal”) from its landlord, which sets out the terms for the surrender of the existing lease and the execution of a new triple-net lease which would expire on October 31, 2014 with a stipulation that the landlord has the right to terminate the lease at any time after November 1, 2012 with nine months notice and amend the lease expiry date accordingly. Under the terms of the Proposal, the minimum rental payment under a new lease would be approximately \$24.4 per month, with annual increases of 2.0%. In addition, per the terms of the Proposal, under a new lease agreement, the Company would be obligated to pay approximately \$478 for rent in arrears prior to the expiry of the new lease; however, the landlord would also agree to release the Company from this obligation provided that the Company is not “in default” throughout the term of a new lease. The Company would also be obligated to make three equal and consecutive monthly payments, not to exceed \$350 in total, commencing on December 31, 2009 for recent repairs made by the landlord to the property. In addition, the Company would agree to complete these repairs prior to September 30, 2010. Under the terms of the Proposal, the Company would continue to be responsible for the maintenance of the property under a new lease.

ATLANTIS SYSTEMS CORP.

Notes to the Interim (Unaudited) Consolidated Financial Statements

September 30, 2009 and 2008

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

The Company did not request a waiver with respect to its non-compliance with certain terms of an agreement with ComVest for the reporting period ended September 30, 2009 in order to avoid the waiver fee (note 12).