

Spectra Inc.
Consolidated Financial Statements
June 30, 2004
Canadian Dollars

REVIEW ENGAGEMENT REPORT

We have reviewed the Consolidated balance sheet of Spectra Inc. as at June 30, 2004 and the statement of operations, deficit and cash flows for the six months then ended. Our review was made in accordance with Canadian generally accepted standards for review engagements and accordingly consisted primarily of enquiry, analytical procedures and discussion related to information supplied to us by the company.

A review does not constitute an audit and consequently, we do not express an audit opinion on these financial statements. Based on our review, nothing has come to our attention that causes us to believe that these financial statements are not, in all material respects, in accordance with Canadian generally accepted accounting principles.

August 26, 2004
Markham, Ontario

Francis & McKinney, LLP
Chartered Accountants

Spectra Inc.
Consolidated Balance Sheet
June 30, 2004
Canadian Dollars

	June 30, 2004	June 30, 2003
Assets		
Current assets:		
Cash	\$ 4,892	\$ 2,337
Accounts receivable	81,779	71,348
Inventory (note 2)	91,074	92,594
Prepaid expenses	<u>19,923</u>	<u>37,800</u>
	<u>197,668</u>	<u>204,079</u>
Capital assets, at cost (note 3)		
Less: accumulated amortization	149,367	165,989
	<u>86,579</u>	<u>94,086</u>
	<u>62,788</u>	<u>71,903</u>
Other assets, at cost (note 4):		
Patent and product rights	510,651	512,358
Development expenses	<u>179,042</u>	<u>262,727</u>
	689,693	775,085
Less: accumulated amortization	<u>555,927</u>	<u>565,015</u>
	<u>133,766</u>	<u>210,070</u>
	<u>\$ 394,222</u>	<u>\$ 486,052</u>

Prepared Without Audit
See the Accompanying Notes

Spectra Inc.
Consolidated Balance Sheet
June 30, 2004
Canadian Dollars

	June 30, 2004	June 30, 2003
Liabilities		
Current liabilities:		
Current portion of loans payable	\$ 29,800	\$ 29,800
Accounts payable and accrued liabilities	<u>1,043,211</u>	<u>533,697</u>
	<u>1,073,011</u>	<u>563,497</u>
Long term liabilities (note 5):		
Loans payable, net of current portion	<u>626,926</u>	<u>618,853</u>
	<u>1,699,937</u>	<u>1,182,350</u>
Shareholders' Deficiency		
Capital account (note 6)	3,853,098	3,798,098
Deficit	<u>(5,158,813)</u>	<u>(4,494,396)</u>
	<u>(1,305,715)</u>	<u>(696,298)</u>
	<u>\$ 394,222</u>	<u>\$ 486,052</u>

Approved By The Board:

Andrew Malion Director

Michael Faye Director

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Spectra Inc.
Consolidated Statement of Operations and Deficit
For the Six Months Ended June 30, 2004
Canadian Dollars

	June 30, 2004	June 30, 2003
Revenues	\$ 276,112	\$ 227,961
Cost of revenue	<u>133,389</u>	<u>86,907</u>
Gross profit	<u>142,723</u>	<u>141,054</u>
Selling, general and administrative expenses:		
Advertising	535	450
Selling expenses	38,115	29,887
Legal, accounting and professional fees	24,753	11,361
Office and general	24,125	23,581
Premises	28,756	28,545
Subcontract labour	37,359	56,419
Interest and financing fees	37,446	33,069
Amortization		
- capital assets	1,561	4,892
- patents and trademarks	44,227	46,036
- development expenses	20,151	11,307
- internet service provider	-	5,500
Product development	-	1,400
Consulting	19,577	19,218
Commission	15,509	15,583
Royalty	14,812	12,448
Management	<u>75,000</u>	<u>75,000</u>
	<u>381,926</u>	<u>374,696</u>
Income (loss) from operations	(239,203)	(233,642)
Income tax (note 9)	<u>-</u>	<u>-</u>
Net income (loss)	(239,203)	(233,642)
Deficit, beginning of period	<u>(4,919,610)</u>	<u>(4,260,754)</u>
Deficit, end of period	<u>\$(5,158,813)</u>	<u>\$(4,494,396)</u>

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Spectra Inc.
Consolidated Statement of Cash Flows
For the Six Months Ended June 30, 2004
Canadian Dollars

	June 30, 2004	June 30, 2003
Operating activities:		
Net income (loss)	\$ (239,203)	\$ (233,642)
Amortization	<u>65,939</u>	<u>67,735</u>
	(173,264)	(165,907)
Changes in non-cash working capital items:		
Decrease (increase) in accounts receivable	(34,649)	(27,023)
Decrease (increase) in inventory	(4,423)	19,836
Decrease (increase) in prepaid expenses	5,216	4,511
(Decrease) increase in accounts payable	<u>203,592</u>	<u>121,337</u>
	<u>(3,528)</u>	<u>(47,246)</u>
Investment activities:		
Capital asset additions	(4,535)	(2,795)
Patent and product rights	<u>(200)</u>	<u>(3,373)</u>
	<u>(4,735)</u>	<u>(6,168)</u>
Financing activities:		
Loan proceeds	2,226	26,888
Issuance of shares	<u>5,000</u>	<u>28,750</u>
	<u>7,226</u>	<u>55,638</u>
Change in cash resources	(1,037)	2,224
Cash resources, beginning of year	<u>5,929</u>	<u>(36,085)</u>
Cash resources, end of period	<u>\$ 4,892</u>	<u>\$ (33,861)</u>

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Notes to Consolidated Financial Statements
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1. Accounting Policies:

The company incorporated under the Laws of the Province of Alberta, follows accounting policies generally accepted in Canada.

Inventory is stated at the lower of cost and net realizable value with cost determined on the first-in, first out method.

Capital assets are stated at and amortized over the estimated useful life of the asset at the following annual rates:

Furniture and fixtures - 20% declining balance
Computer equipment - 30% declining balance
Equipment - 20% declining balance
Dies and molds - units of production
Patents - straight line over the life of the patent
Development expenses - 5 year straight line

In the year of acquisition, one-half of the above rates are charged.

2. Inventory:

Inventory consists of:

	2004	2003
Finished product	\$ 18,184	\$ 20,447
Raw materials	<u>72,890</u>	<u>72,147</u>
	<u>\$ 91,074</u>	<u>\$ 92,594</u>

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3. Capital Assets:

Capital assets consist of:

	June 30, 2004			2003
	Cost	Accumulated Amortization	Net	Net
Dies and molds	\$ 89,405	\$ 39,433	\$ 49,972	\$ 52,852
Furniture & fixtures	21,194	18,206	2,988	3,736
Computer equipment	10,744	8,654	2,090	2,986
Plant & equipment	28,024	20,286	7,738	12,329
	\$ 149,367	\$ 86,579	\$ 62,788	\$ 71,903

4. Other Assets:

Other assets consist of development expenses, product rights and patents which have been deferred and will be charged to future operations.

	June 30, 2004			2003
	Cost	Accumulated Amortization	Net	Net
Product rights	\$ 18,000	\$ 11,700	\$ 6,300	\$ 8,100
Patents and trademarks	492,651	421,535	71,116	153,984
Development expenses	179,042	122,692	56,350	47,986
	\$ 689,693	\$ 555,927	\$ 133,766	\$ 210,070

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5. Loans Payable:

The company has a demand loan with TD Canada Trust bearing interest at prime plus one percent repayable over a five year term. A working capital loan has been secured with the Business Development Bank of Canada over a five year period, bearing interest at a floating rate currently 11.5 percent, both loans are secured with a general security agreement and personal guarantees from Management (Andrew Malion and Michael Faye). Loans from Management bear interest at 6.0% per annum. These loans are secured with a general security agreement including a fixed charge on the Schandelmeir patent.

Balances at June 30 are:	2004	2003
TD Canada Trust	\$ 26,162	\$ 36,198
Business Development Bank of Canada	46,200	61,050
Management loans	<u>584,364</u>	<u>551,405</u>
	656,726	648,653
Less current portion	<u>29,800</u>	<u>29,800</u>
	<u>\$ 626,926</u>	<u>\$ 618,853</u>

The aggregate amount of payments required to repay the Business Development Bank

Of Canada and TD Canada Trust in each of the next five fiscal years are:

2004 -	\$ 22,377
2005 -	29,836
2006 -	26,536
2007 -	<u>1,072</u>
	<u>\$ 79,821</u>

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6. Capital Account:

Authorized share capital - unlimited number of common voting shares, first, second, third and fourth preference shares.

Issued share capital:	6/30/04	6/30/03
28,966,837(2003 - 28,416,837) common shares for	\$3,826,098	\$3,771,098
90,000 (2003 - 90,000) Spectra preference shares for	<u>27,000</u>	<u>27,000</u>
	<u>\$3,853,098</u>	<u>\$3,798,098</u>

	Common Shares	
	#	\$
Common shares issued December 31, 2001	27,951,837	\$ 3,724,848
Issued during 2002	<u>265,000</u>	<u>17,500</u>
Balance, December 31, 2002	28,216,837	3,742,348
Issued during 2003	<u>700,000</u>	<u>78,750</u>
Balance, December 31, 2003	28,916,837	3,821,098
Issued during 2004	<u>50,000</u>	<u>5,000</u>
Balance June 30, 2004	<u>28,966,837</u>	<u>\$ 3,826,098</u>

7. Rent Commitment:

The company is obligated under an operating lease for premises until February 28, 2007 as follows:

2004	\$ 50,726
2005	50,892
2006	50,892
2007	<u>8,482</u>
	<u>\$ 160,992</u>

8. Royalties:

Spectra Products Inc. has obligations to pay minimum royalties of \$ 80,000 per annum

until August 6, 2004 for the Brake Safe product (refer to Subsequent Event Note 12).

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9. Income Tax Losses:

The consolidated group of companies has tax losses available for carry forward totaling \$3,538,869. These losses expire as follows:

2004	\$ 944,235
2005	166,241
2006	16,680
2007	338,375
2008	727,377
2009	677,105
2010	<u>658,856</u>
	<u>\$3,528,869</u>

The potential benefit of these losses have not been recognized in the accounts. There are no significant timing differences between accounting and taxable income.

10. Earnings Per Share:

Earnings per share for the last full fiscal years are as follows:

	2003	2002
Earnings (loss) per share	\$ (.0228)	\$ (.0240)
Earnings (loss) per share fully diluted	\$ (.0216)	\$ (.0227)

11. Segment Information:

The company operates in one market segment – bus and truck transportation safety equipment. Spectra Products Inc. manufactures and markets brake monitoring equipment as an after market product through transportation dealers, distributors, and direct sales to fleet operators.

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12. Subsequent Event:

On August 6, 2004 Spectra Inc. closed a debenture financing arrangement with Dynamic Venture Opportunities Fund Ltd. (“DVOF”), an Ontario labour-sponsored venture capital fund, whereby DVOF advanced \$ 750,000 to Spectra Inc.’s wholly-owned subsidiary, Spectra Products Inc. (“SPI”). In consideration of the advance of these funds, DVOF is entitled to receive royalty payments equal to the greater of \$100,000 per annum or 10% of the total annual gross revenue generated by SPI. Twenty-five percent of each royalty payment shall be allocated against the principal amount of the debenture. The royalty payment shall continue at 10% of SPI’s gross revenue until the earlier of (i) the date that the Royal Debenture has been fully repaid; and (ii) 15 years from issue date, at which time any remaining principal amount shall be due. As additional consideration, Spectra Inc. issued 3,000,000 bonus shares to DVOF at a deemed price of \$0.05 per share, representing a deemed value equal to 20% of the \$ 750,000 invested.