

**Spectra Inc.**  
**Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**Revised January 31, 2006**

## **Auditor's Report**

To the Shareholders of:  
**Spectra Inc.**

We have audited the consolidated balance sheets of Spectra Inc. as at December 31, 2004 and December 31, 2003 and the consolidated statements of income, deficit and changes in cash flows for each of the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and December 31, 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

**Francis & McKinney, LLP.**  
**Chartered Accountants.**

**April 27, 2005**  
**Markham, Ontario**

**Spectra Inc.**  
**Consolidated Balance Sheet**  
**December 31, 2004**  
**Canadian Dollars**

	<b>Dec. 31, 2004</b>	<b>Dec. 31, 2003</b>
<b>Assets</b>		
Current assets:		
Cash	\$ 7,915	\$ 5,929
Accounts receivable	124,604	49,439
Inventory (note 2)	147,419	86,651
Prepaid expenses	<u>25,383</u>	<u>25,139</u>
	<u>305,321</u>	<u>167,158</u>
Capital assets, at cost (note 4)	167,237	163,194
Less: accumulated amortization	<u>98,741</u>	<u>98,845</u>
	<u>68,496</u>	<u>64,349</u>
Other assets, at cost (note 5):		
Patent and product rights	513,180	510,116
Development expenses	201,310	325,727
Prepaid royalty and financing	<u>218,250</u>	<u>-</u>
	932,740	835,843
Less: accumulated amortization	<u>650,314</u>	<u>642,434</u>
	<u>282,426</u>	<u>193,409</u>
	<u>\$ 656,243</u>	<u>\$ 424,916</u>

**See the Accompanying Notes**

**Spectra Inc.**  
**Consolidated Balance Sheet**  
**December 31, 2004**  
**Canadian Dollars**

	<b>Dec. 31, 2004</b>	<b>Dec. 31, 2003</b>
<b>Liabilities</b>		
Current liabilities:		
Current portion of loans payable	\$ 129,836	\$ 29,836
Accounts payable and accrued liabilities	<u>821,349</u>	<u>844,628</u>
	<u>951,185</u>	<u>874,464</u>
Long term liabilities (notes 6):		
Loans payable, net of current portion	<u>1,083,851</u>	<u>624,664</u>
	<u>2,035,036</u>	<u>1,499,128</u>
<b>Shareholders' Deficiency</b>		
Capital account (note 7)	4,053,098	3,848,098
Deficit	<u>(5,431,891)</u>	<u>(4,922,310)</u>
	<u>(1,378,793)</u>	<u>(1,074,212)</u>
	<u>\$ 656,243</u>	<u>\$ 424,916</u>

**Approved By The Board:**

Andrew Malion Director

Michael Faye Director

**See the Accompanying Notes**

**Spectra Inc.**  
**Consolidated Statement of Operations and Deficit**  
**For the Year Ended December 31, 2004**  
**Canadian Dollars**

	<b>Dec. 31, 2004</b>	<b>Dec. 31, 2003</b>
Revenues	\$ 699,640	\$ 445,052
Cost of revenue	<u>289,046</u>	<u>201,222</u>
Gross profit	<u>410,594</u>	<u>243,830</u>
Selling, general and administrative expenses:		
Advertising	2,704	1,160
Royalty debenture	32,443	-
Selling expenses	66,338	81,420
Legal, accounting and trustee fees	80,080	57,074
Office and general	56,940	42,601
Premises	56,109	55,424
Subcontract labour	58,890	108,250
Interest on long term debt	85,674	68,114
Amortization		
- capital assets	6,176	41,710
- patents and trademarks	80,198	81,014
- development expenses	48,692	-
- internet service provider	-	33,000
Product development	10,919	1,400
Public relations	-	1,125
Consulting	61,115	20,936
Commission	31,892	31,900
Royalty	44,705	112,558
Management	<u>200,000</u>	<u>165,000</u>
	<u>922,875</u>	<u>902,686</u>
Income (loss) from operations	(512,281)	(658,856)
Income tax (note 8)	<u>-</u>	<u>-</u>
Net income (loss)	(512,281)	(658,856)
Deficit, beginning of year	<u>(4,919,610)</u>	<u>(4,263,454)</u>
Deficit, end of year	<u>\$(5,431,891)</u>	<u>\$(4,922,310)</u>
Earnings (loss) per share basic (Note 7,9)	(0.0142)	(0.0228)
Earnings (loss) per share fully diluted	(0.0137)	(0.0211)

**See the Accompanying Notes**

**Spectra Inc.**  
**Consolidated Statement of Cash Flows**  
**For the Year Ended December 31, 2004**  
**Canadian Dollars**

	<b>Dec. 31, 2004</b>	<b>Dec. 31, 2003</b>
Operating activities:		
Net income (loss)	\$ (424,796)	\$ (658,856)
Amortization	135,066	155,724
Interest paid, net	<u>(87,485)</u>	<u>-</u>
	<u>(377,215)</u>	<u>(503,132)</u>
Changes in non-cash working capital items:		
Decrease (increase) in accounts receivable	(75,165)	(5,114)
Decrease (increase) in inventory	(60,768)	25,779
Decrease (increase) in prepaid expenses	(244)	17,172
(Decrease) increase in accounts payable	<u>(20,579)</u>	<u>426,868</u>
	<u>(533,971)</u>	<u>(38,427)</u>
Investment activities:		
Capital asset additions	(10,324)	-
Patent, product rights and other	(247,782)	(64,131)
Reduction in management loans	<u>(150,883)</u>	<u>-</u>
	<u>(408,989)</u>	<u>(64,131)</u>
Financing activities:		
Loan proceeds	739,946	24,607
Issuance of shares	<u>205,000</u>	<u>78,750</u>
	<u>944,946</u>	<u>103,357</u>
Change in cash resources	1,986	799
Cash resources, beginning of year	<u>5,929</u>	<u>5,130</u>
Cash resources, end of year	<u>\$ 7,915</u>	<u>\$ 5,929</u>

**See the Accompanying Notes**

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**1. Nature of Business and Basis of Presentation:**

**Nature of Business –**

Spectra Inc. is a manufacturing and marketing company incorporated under the laws of the Province of Ontario on December 18, 1996. The Company operates in

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

**Basis of Presentation –**

These financial statements have been prepared on a going concern basis which presumes the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future.

The Company has experienced operating losses and at December 31, 2004 has a working capital deficiency of \$ 645,864. The Company's ability to continue operations is dependent upon its ability to achieve profitability, maintain current financing and obtain new sources of financing. The outcome of these matters cannot be predicted at this time. The financial statements do not include any adjustments to the amounts and classification of assets and liabilities that might be necessary should the Company be unable to continue operations.

**2. Significant Accounting Policies:**

The Company follows accounting policies generally accepted in Canada. The following is a summary of significant accounting policies used in the preparation of these financial statements:

**Use of estimates:**

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

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

Inventory:

Inventory is valued at the lower of cost, determined on a first-in, first- out basis, and net realizable value. Cost consists of raw material and direct labour.

Capital Assets:

Capital assets are carried at cost. Amortization is provided over the assets estimated useful life as follows:

Dies and molds - units of production method  
Furniture and fixtures - 20 % declining balance method  
Computer equipment - 30 % declining balance method  
Plant equipment - 20 % declining balance method

Annually, or more frequently as circumstances require, (such as a decrease in sales prices, an increase in operating costs), reviews are undertaken to evaluate

the carrying values of capital assets. Effective January 1, 2004 the Company prospectively adopted the requirements of CICA 3063 "Impairment of Long-lived Assets" to evaluate impairment. If it is determined that the future cash flows from a property are less than its carrying value, a write-down to the estimated fair value is made with a charge to earnings. Adoption of CICA 3063 had no effect on these financial statements.

The Company's estimated of future cash flows are subject to risks and uncertainties.

It is reasonably possible that changes in estimates could occur which may affect the expected recoverability of the Company's investment in capital assets.

Other Assets:

Other assets are carried at cost. Amortization is provided over the assets estimated useful life as follows:

Patents and Product Rights - Straight line method over the term of the asset.  
Prototypes - Straight line, 3 years.  
Finance fee - Straight line over term of debenture.  
Prepaid Royalty - straight line over original term of royalty agreement.

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

Revenue recognition:

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or the services have been rendered, the sales price is fixed or determinable and collection of the related receivable is reasonably assured. Title and risk of loss generally pass to the customer at the time of delivery of the product to a common carrier. Revenue is recognized upon delivery,

provided that fulfillment of acceptance criteria can be demonstrated prior to shipment. The Company considers the receipt of a purchase order in writing or verbally together with a signed packing slip or bill of lading as persuasive evidence that an arrangement exists provided the customer is purchasing C.O.D. or is credit worthy. Based on these circumstances the customer is invoiced and the receivable is booked. The Company permits customer returns subject to a restocking charge and issues a credit to the customer. The returned product is entered into inventory.

Share Options:

The Company values options based on the trading price of the Company's common shares on the date of the grant, (CICA Handbook section 3870, *Stock-based compensation and other stock-based payments*).

Financial instruments:

The Company's financial instruments consists of cash, accounts receivable, bank indebtedness, accounts payable and accrued liabilities and loans payable. Unless otherwise stated the fair value of the financial instruments approximates their carrying value.

**3. Inventory:**

Inventory consists of:

	<u>2004</u>	<u>2003</u>
Product for resale	\$ 35,712	\$ 14,170
Raw materials	<u>111,707</u>	<u>72,481</u>
	<u>\$ 147,419</u>	<u>\$ 86,651</u>

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**4. Capital Assets:**

Capital assets consist of:

	2004			2003
	Cost	Accumulated Amortization	Net	Net
Dies and molds	\$ 96,191	\$ 42,135	\$ 54,056	\$ 49,972
Furniture & fixtures	24,731	18,892	5,839	3,320
Computer equipment	10,744	9,023	1,721	2,459
Plant & equipment	28,024	21,144	6,880	8,598
	\$ 159,690	\$ 91,194	\$ 68,496	\$ 64,349

Amortization of capital assets consists of:

	2004	2003
Office furniture and fixtures	\$ 1,018	\$ 830
Machinery, plant and equipment	1,718	2,150
Computers	738	1,053
Dies and molds	2,702	5,741
	\$ 6,176	\$ 9,774

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**5. Other Assets:**

Other assets include development costs which have been deferred and will be charged to future operations.

Other assets consist of:

	2004			2003
	Cost	Accumulated Amortization	Net	Net
Patents and trademarks	\$ 495,180	\$ 466,174	\$ 29,006	\$ 113,908
Product rights	18,000	12,600	5,400	7,200
Deferred charges	207,697	207,697	-	9,301
Prototypes	89,468	29,822	59,646	63,000
Royalty Deb. Finance Fee	68,388	2,280	66,108	-
Prepaid Royalty Brake Safe Inc.	149,862	27,596	122,266	-
Internet service provider	55,000	55,000	-	-
	<u>\$1,083,595</u>	<u>\$ 801,169</u>	<u>\$ 282,426</u>	<u>\$ 193,409</u>

Amortization of other assets consists of:

	2004	2003
Deferred charges	\$ 9,301	\$ 22,368
Product rights – Brake Safe	1,800	1,800
Patent and trademarks	87,966	88,782
Software and prototype	29,823	-
Internet service provider	-	33,000
	<u>\$128,890</u>	<u>\$145,950</u>

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**6. Loans Payable:**

A working capital loan has been secured with the Business Development Bank of Canada repayable over a five year period, bearing interest at a floating rate currently 11.5%. This loan is secured by a general security agreement and personal guarantees from Management (Andrew Malion and Michael Faye). Loans from management total \$ 416,297 and bear interest at 9.0% per annum. These loans are secured with a general security agreement including a fixed charge on the Schandelmeier patent. The management loans are repayable 366 days after demand.

The aggregate amount of payments required to repay the Business Development Bank of Canada in each of the next five years are:

2005	\$ 19,800
2006	<u>16,500</u>
	<u>\$ 36,300</u>

The Company's operating line with the TD Canada Trust for \$ 50,000 was converted into a demand loan payable over 60 months beginning February 28, 2002 bearing interest at prime plus one percent. This loan is secured with general security agreement. The balance at December 31, 2004 is \$ 21,144. The amount due in each of the following next three years is as follows:

2005	\$ 10,036
2006	10,036
2007	<u>1,072</u>
	<u>\$ 21,144</u>

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.

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

The minimum amount due in each of the next five years is as follows:

2005	100,000
2006	100,000
2007	100,000
2008	100,000
2009	100,000

	<u>2004</u>	<u>2003</u>
Business Development Bank of Canada	\$ 36,300	\$ 56,100
Management loans	416,297	567,220
TD Canada Trust	21,144	31,180
Dynamic Venture Opportunities Fund	<u>739,946</u>	<u>-</u>
	1,213,687	654,500
Less current portion	<u>129,836</u>	<u>29,836</u>
	<u>\$ 1,083,851</u>	<u>\$ 624,664</u>

**7. Capital Account:**

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

Issued share capital:	12/31/04	12/31/03
35,966,837(2003 - 28,916,837) common shares for	\$4,026,098	\$3,821,098
90,000 (2003 - 90,000) Spectra preference shares for	<u>27,000</u>	<u>27,000</u>
	<u>\$4,053,098</u>	<u>\$3,848,098</u>
	<b>#</b>	<b>\$</b>
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>7,050,000</u>	<u>205,000</u>
Balance, December 31, 2004	<u>35,966,837</u>	<u>\$ 4,026,098</u>

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**Share Options:**

The Company has a stock option plan that permits the grant of options to directors, officers, employees and consultants. The plan provides for the grant of a maximum number of options equal to ten percent of issued and outstanding common shares issued with maximum term of five years, fully vested at date of grant. The company values options based on the trading price of the Company's common shares on the date of the grant, (CICA Handbook section 3870, *Stock-based compensation and other stock-based payments*), and the pricing requirements of the TSX Venture Exchange. The table below lists Options granted for the fiscal year ending December 31, 2004.

Expiry Date	Number of Options Granted	Exercise Price	Remaining Contractual Life
March 2, 2005	450,000	\$0.10	0.2 years
October 11, 2005	125,000	\$0.16	0.8 years
January 10, 2006	250,000	\$0.25	2.0 years
January 7, 2007	25,000	\$0.20	3.0 years
January 15, 2007	350,000	\$0.20	3.0 years
March 2, 2008	800,000	\$0.10	3.2 years

**8. Income Taxes:**

The consolidated group of companies has income tax losses available for carry forward of \$ 2,643,001. Losses expire as follows:

2005	22,262
2006	107,479
2007	373,125
2008	583,363
2009	526,948
2010	643,521
2011	<u>386,303</u>
	<u>\$2,643,001</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.

**Spectra Inc.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2004**  
**Canadian Dollars**

**9. Earnings per share:**

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

	<b>2004</b>	<b>2003</b>
Earnings (loss) per share basic	\$ (.0142)	\$ (.0228)
Earnings (loss) per share fully diluted	\$ (.0137)	\$ (.0211)

**10. Commitments:**

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

2005	\$ 50,892
2006	50,892
2008	<u>8,482</u>
	<u>\$ 110,266</u>