



# **Fireswirl**

## **Technologies Inc.**

**Management Discussion and Analysis of  
Financial Condition and Results of Operations**

**For the three and six months ended June 30, 2012 and 2011**

**August 22, 2012**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following Management Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with Fireswirl Technologies Inc. ("Fireswirl" or the "Company") interim consolidated financial statements and the accompanying notes for the period ended June 30, 2012 which have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Additional information about the Company is available on SEDAR at ([www.sedar.com](http://www.sedar.com)) under Fireswirl Technologies Inc. and on the Company website at [www.fireswirl.com](http://www.fireswirl.com).

**Special Note Regarding Forward Looking Statements**

This MD&A contains certain forward looking statements which reflect management's expectations regarding the Company's growth, results of operations, performance and business prospects and opportunities.

Statements about the Company's future plans and intentions, results, level of activity, performance or achievements or other future events constitute forward looking statements. Whenever possible, words such as "anticipate", "estimate", "may", "will", "could", "should", "expect", "plan", "intend", "believe", "estimate", or "potential" or similar words, have been used to identify these forward looking statements.

The Company cautions that the forward-looking statements reflect the current views and/or expectations of the Company with respect to its performance, business and future events. Investors are cautioned that all forward looking statements involve risks, uncertainties and assumptions. Including, without limitations, those relating to a limited operating history, an uncertain regulatory environment, a competitive environment, internet viability and system infrastructure and reliability, dependence on key personnel and foreign exchange fluctuations. These risks may cause the Company's actual results to differ materially from those projected in the forward looking statements. The Company does not undertake any obligations to release publicly any revisions for updating any voluntary forward looking statements.

Factors which could cause results or events to differ from current expectations include among other things: the impact of government legislation; the impact of competition; the ability of the Company to retain and attract qualified professionals; the impact of rapid technological and market change; loss of business or credit risk with current and perspective major customers; general industry and market conditions, growth rates and currency rate fluctuations. The Company disclaims any intentions or obligations to update or revise any forward looking statements, whether as a result of new information, future events or otherwise, except as required by law. No assurance can be given that actual results, performance or achievement expressed or implied by forward looking statements within this disclosure will occur; or if they do, that any benefits can be derived from them.

Past performance has been considered in drawing conclusions with respect to forward looking statements contained in this MD&A.

## **OVERVIEW**

Fireswirl Technologies Inc. (TSX Venture: FSW; “the Company”) was founded in 1999 and operated as a software development and project management company specializing in payment platforms and online gaming software for the internet. In 2006, the Company became a publically listed company through a reverse takeover and a \$3.2 million equity financing accompanying its qualifying transaction.

In 2007, the Company formed its first wholly owned subsidiary in China to explore the rapidly emerging market. The Company has since increased its business presence in the country gradually.

In 2009, the Company successfully completed its acquisition of 50% of all rights and interests of Beijing Xingchang Xinda Technology Development Co., Ltd. (“XCXD”), an e-commerce outsourcing and fulfillment solution provider in China, in consideration for 6,058,673 common shares of the Company. Fireswirl has majority voting rights and majority board control over XCXD according to the agreements related to the transaction.

## **CORPORATE SUMMARY**

XCXD is a leader in the branded online store outsourcing market for mobile handsets in China. XCXD is currently the exclusive operator of the official online store and the Taobao Flagship Store for Nokia, Motorola, Sony Mobile and HTC in China. XCXD is also expanding its business into other product categories, such as computer accessories, toys and apparels. XCXD has recently become the sole operator of the official online store and the Taobao Flagship Store for Toys“R”Us, an international toy retailer. It is also the sole operator of the Taobao Flagship Store for LEGO, an international toy brand, and Casio, a well-known maker of watches and compact digital cameras. The company also signed a partnership with GSI Commerce to expand its footprint in China.

Fireswirl is continuing to execute on its long-term plan to becoming the largest e-commerce service platform in China for international brands, providing the technology and fulfillment know-how for these brands to break into the country’s rapid growing e-commerce market.

China, being the predominant geographic location for Fireswirl, has over 1.3 billion people in population and is the fastest growing major economy in the world. To this end, the business opportunities in China are enormous. The e-commerce market in China continues to expand at a rapid rate. According to the China Internet Network Information Centre, there were 513 million Internet users in China at the end of 2011, which has grown by 12.3% compared to the same period in 2010. The number of Internet shopper has also grown from 161 million in 2010 to 194 million in 2011, representing an increase of 20.8%.

Fireswirl’s core business is to operate the “official online store” in China on behalf of international brands it has contractual agreements with, thus it is not in direct competition with most other online retailers who do not represent any particular brand and sell products from a variety of brand names. The Company generates its revenue mainly from reselling branded products on the respective official branded online stores it operates. Due to customer brand loyalty and trust, the Company’s online stores attract natural traffic and strong organic growth without investing heavily into initial marketing. As a result, management views this as a major competitive advantage over other online retailers in China. As China e-commerce is becoming a priority for many international brands, the partnerships between these brands and Fireswirl is an important part of the company’s sustainable growth strategy.

In light of its focus previously on mobile phone products and its reliance on a store of a certain mobile phone brand, the Company started diversifying into both the types of products and also the number of brands in its portfolio during 2011. The strategy has successfully reduced the negative impact to the

company when one of its key mobile phone brands in its portfolio suffered a significant drop in market-share and brand value. Since late 2011, the company has been steadily adding a number of major international brands into its portfolio and also diversified into various product categories.

For each new brand that launches a branded online store, it is typical for the new store to take anywhere between nine months to one year to gain market acceptance before it shows meaningful growth in sales. To that end, Fireswirl believes that its branded stores launched since the end of 2011 and the new branded stores in the current pipeline shall support the long-term growth of the Company.

The Company's goal is to achieve economies-of-scale by increasing the number of brands it signs up in growing overall recurring revenues, to achieve profitability. All branded official online stores the Company operates are running on the same technology platform, and will leverage off the Company's existing resources including data infrastructure, warehouse management and administrative support base. Economies of scale are achieved as the cost per transaction can be substantially reduced as high transaction volume is obtained.

## **SUMMARY OF FINANCIAL RESULTS**

### **Key Financial Events**

- Total operating revenue increased to \$5,830,178 and \$9,318,019 for the three and six months ended June 30, 2012 compared to \$5,001,975 and \$9,178,947 during the same period in 2011, representing an increase of 16.6% and 1.5%. Merchandise revenue increased by 11.2% and decreased 3.5% during the three and six months ended June 30, 2012 respectively compared to the same period in 2011. Service revenue increased by 285.2% and 391.5% respectively during the three and six months ended June 30, 2012 compared to the same period in 2011.
- Total operating expense was \$5,891,080 and \$9,520,852 for the three and six months ended June 30, 2012 compared to \$5,534,519 and \$9,841,298 for the same period of 2011, representing an increase of 6.4% and a decrease of 3.3% respectively. The increase was mainly due to the increase in cost of sales related expenses corresponding to increase in revenue and an increase in all operating expense due to expansion of business into other sectors than cellphone sales.
- The Company reported a comprehensive loss on common shares of \$204,731 and \$231,318 for the three and six month period ended June 30, 2012 compared to a comprehensive loss on common share of \$382,847 and \$607,936 for the same period of 2011, representing an decrease in loss of 46.5% and 62% respectively.
- Fully diluted loss per share was \$0.00 and \$0.01 for the three and six month period ended June 30, 2012 compared to fully diluted losses of \$0.01 and \$0.02 for the same period of 2011.
- As at June 30, 2012, the Company had cash and cash equivalents (including restricted cash) of \$2,152,400 compared to \$1,772,477 as at December 31, 2011, representing an increase of 21.4%. As at June 30, 2012, the Company had working capital of \$671,904 compared to \$1,005,472 as at December 31, 2011, representing a decrease of 33.2%. The Company had long term debt of \$nil as at June 30, 2012 compared to \$nil as at December 31, 2011.

## Marketing Highlights

- The Company's subsidiary, Beijing Xingchang Xinda Technology Development Co., Ltd. ("XCXD"), was appointed by General Imaging (SZ) Co. Ltd to exclusively operate its online flagship store on Taobao Mall ("Tmall"), the largest online B2C shopping portals in China, to market and sell General Electric, or GE, branded digital cameras and relevant photography products.
- The company announced a partnership with GSI Commerce ("GSI"), an EBAY company, to enable GSI's e-commerce services in China. GSI serves more than 1,000 retailers and global brands worldwide to provide e-commerce technology, fulfillment, customer care and marketing services.
- The company announced that its two subsidiaries, Fireswirl Asia Limited and XCXD, have jointly signed an agreement with Toys"R"Us Retailing (China) Limited ('Toys"R"Us, China') to provide e-commerce operation service, including to its Taobao Flagship Store in China.
- The company announced that its subsidiary, XCXD has signed an agreement with A.O.Smith (China) Water Heater Co., Ltd. ("A.O. Smith China") to exclusively operate its e-commerce platform in China. A.O. Smith is one of the world's leading manufacturers of residential and commercial water heating equipment, offering a comprehensive product line featuring the best-known brands in North America and China.

## SELECTED QUARTERLY FINANCIAL DATA

The following table sets out selected unaudited financial information of the Company on a consolidated basis for the last eight quarters.

	Q2 2012	Q1 2012	Q4 2011	Q3 2011	Q2 2011	Q1 2011	Q4 2010	Q3 2010
<b>Operating revenues</b>								
Sales Revenue	5,452,645	3,296,332	4,567,746	5,631,757	4,903,963	4,159,212	6,356,033	4,612,967
Advertising Revenue	-	-	-	-	-	-	23,868	22,767
Service Revenue	377,533	191,509	334,102	325,724	98,012	17,760	205,147	108,093
	5,830,178	3,487,841	4,901,849	5,957,481	5,001,975	4,176,972	6,585,048	4,743,827
Other operating income	-	-	-	-	-	-	30	-
<b>Total operating income</b>	<b>5,830,178</b>	<b>3,487,841</b>	<b>4,901,849</b>	<b>5,957,481</b>	<b>5,001,975</b>	<b>4,176,972</b>	<b>6,585,078</b>	<b>4,743,827</b>
<b>Operating expenses</b>								
Purchases	4,817,550	2,579,114	3,681,088	5,016,399	4,683,332	3,600,724	5,726,577	3,934,968
Delivery charges	90,073	164,372	324,828	151,420	140,694	75,697	133,298	104,689
Other related expense	162,001	127,915	303,957	116,619	85,394	57,501	90,980	110,287
Foreign exchange (gain)/loss	475	797	-	-	-	-	83,515	4,731
Amortization	40,333	40,159	39,754	39,946	42,915	38,815	19,522	19,611
Sales and marketing	47,637	33,740	44,982	49,736	27,439	26,485	82,317	51,185
General administration	247,592	214,250	215,500	247,435	183,613	174,152	328,355	290,143
Salaries and benefits	463,042	444,663	499,499	436,202	365,852	331,955	466,386	412,557
Share-based payment expense	22,377	22,377	85,204	17,930	-	-	904	2,050
Impairment	-	2,385	-	-	5,280	1,450	-	-
Bad Debt Expense	-	-	-	-	-	-	1,492	-
<b>Total Operating Expense</b>	<b>5,891,080</b>	<b>3,629,771</b>	<b>5,194,812</b>	<b>6,075,687</b>	<b>5,534,519</b>	<b>4,306,779</b>	<b>6,933,347</b>	<b>4,930,221</b>
<b>Operating Income/(Loss)</b>	<b>(60,902)</b>	<b>(141,931)</b>	<b>(292,964)</b>	<b>(118,206)</b>	<b>(532,544)</b>	<b>(129,807)</b>	<b>(348,270)</b>	<b>(186,394)</b>
Finance income	2,897	2,718	2,789	4,712	2,357	1,644	6,231	489
Finance costs	(113,582)	(85,301)	(16,066)	(92,241)	(68,495)	(63,915)	(57,112)	(26,116)
<b>Income/(loss) before income tax</b>	<b>(171,587)</b>	<b>(224,514)</b>	<b>(306,241)</b>	<b>(205,735)</b>	<b>(598,682)</b>	<b>(192,078)</b>	<b>(399,151)</b>	<b>(212,021)</b>
Income tax recovery (expenses)	(15,313)	-	(37)	(8,915)	-	(4,551)	-	(35,805)
<b>Net income/(loss)</b>	<b>(186,900)</b>	<b>(224,514)</b>	<b>(306,278)</b>	<b>(214,650)</b>	<b>(598,682)</b>	<b>(196,629)</b>	<b>(399,151)</b>	<b>(247,826)</b>
Other comprehensive income/(loss)								
Foreign exchange currency adjustment	11,294	(197,419)	(15,037)	294,052	28,905	(26,194)	45,261	(4,731)
<b>Comprehensive income/(loss)</b>	<b>(175,606)</b>	<b>(421,932)</b>	<b>(321,315)</b>	<b>79,402</b>	<b>(569,777)</b>	<b>(222,823)</b>	<b>(353,890)</b>	<b>(252,557)</b>
Net income/(loss) attribute to:								
Common shares	(218,273)	(227,764)	(260,667)	(224,732)	(403,356)	(203,904)	(286,522)	(272,827)
Non-controlling interest	31,373	3,250	(45,610)	10,082	(195,326)	7,275	(112,628)	25,001
	(186,900)	(224,514)	(306,278)	(214,650)	(598,682)	(196,629)	(399,151)	(247,826)
Comprehensive income/(loss) attributable to:								
Common shares	(204,732)	(337,576)	(272,687)	(30,933)	(382,846)	(225,090)	(241,261)	(277,558)
Non-controlling interest	29,125	(84,357)	(48,628)	110,335	(186,930)	2,267	(112,628)	25,001
	(175,606)	(421,932)	(321,315)	79,402	(569,777)	(222,823)	(353,890)	(252,557)
<b>Basic/Diluted income/(loss) per share</b>	<b>\$ -</b>	<b>\$ (0.01)</b>	<b>\$ (0.01)</b>	<b>\$ (0.00)</b>	<b>\$ (0.01)</b>	<b>\$ (0.01)</b>	<b>\$ (0.01)</b>	<b>\$ (0.01)</b>

## QUARTERLY RESULTS

### Comparison of the three and six month period ended June 30, 2012 and June 30, 2011

#### Revenue

The Company reported total operating revenue of \$5,830,178 and \$9,318,019 for the three and six months ended June 30, 2012 compared to \$5,001,975 and \$9,178,947 for the same period in 2011, representing an increase of 16.6% and 1.5% due to an increase in merchandise revenue by 11.2% and a decrease of 3.5% respectively. The decrease in merchandise revenue for the six months period is mainly due to a decrease in demand for certain mobile phone brand compensated by the introduction of digital and other products revenues. There is an increase in service revenue by 285.2% and 391.5% respectively compare

to the same period in 2011. The increase in service revenue is mainly due to the increase in setup, customization and software development fee for new brands joining our platform to launch their branded online store.

The breakdown of the Company's revenues by category for the three and six months ended June 30, 2012 and 2011 are as follow:

	Three months ended		Six months ended	
	30-Jun-12	30-Jun-11	30-Jun-12	30-Jun-11
Merchandise resale and trading	\$ 5,452,645	\$ 4,903,963	\$ 8,748,977	\$ 9,063,174
Service and software fees	377,533	98,012	569,042	115,773
<b>Total Revenue</b>	<b>5,830,178</b>	<b>5,001,975</b>	<b>9,318,019</b>	<b>9,178,947</b>
Purchases	4,817,550	4,683,332	7,396,664	8,284,056
Delivery charges	90,073	140,694	254,445	216,391
Other related expense	162,001	85,394	289,916	142,895
<b>Total Cost of Goods Sold</b>	<b>5,069,624</b>	<b>4,909,420</b>	<b>7,941,025</b>	<b>8,643,342</b>
<b>Gross profit</b>	<b>\$ 760,554</b>	<b>\$ 92,555</b>	<b>\$ 1,376,994</b>	<b>\$ 535,605</b>

During the six month period ended June 30, 2012, the Company recognized \$8,748,977 (same period 2011: \$9,063,174) of revenue from the online merchandise sales in China with associated cost of goods sold of \$7,941,025 (same period 2011: \$8,643,342) resulting in the gross profit margin on merchandise sales of 9.2% (same period 2011: 4.6%).

The Company recognized \$569,042 (same period 2011: \$115,773) of revenue from service and maintenance fees during the six month period ended June 30, 2012.

### Operating Expenses

Previously, Canadian GAAP did not provide the same level of specificity of expense analysis. IFRS-IASB requires that expenses be presented using either a nature approach or a function approach; the Company has selected the nature approach. Therefore, cost of good sold is being included in the Operating expense section.

Total operating expenses increased to \$5,891,080 and \$9,520,852 for the three and six month period ended June 30, 2012 compared to \$5,534,519 and \$9,841,298 for the same period of 2011, representing a increase of 6.4% and a decrease of 3.3%.

### Cost of Good Sold

Previously, cost of goods sold was presented as a separate line item under GAAP which includes the cost of purchasing the merchandise, sales tax, delivery, technical service and advertising expenses related to the sales. As we have chosen to present expense using the nature approach under IFRS, cost of goods sold is presented as change in inventory, delivery charges and other related expenses under operating expenses.

The overall cost of good sold increased to \$5,069,624 and \$7,941,025 for the three and six month period ended June 30, 2012 compared to \$4,909,420 and \$8,643,342 for the same period of 2011, representing an increase of 3.3% and a decrease of 8.1% respectively. For the six month period ended June 30, 2012, the decrease is mainly due to a decrease in inventory by 10.7% offset by an increase in other related expenses by 103%.

## **Depreciation and Amortization**

The Company reported depreciation and amortization expense of \$40,333 and \$80,493 for the three and six month period ended June 30, 2012 compared to \$42,915 and \$81,730 for the same period of 2011, representing a decrease of 6% and 1.5% respectively. This decrease is due to minor exchange difference.

## **Sales and Marketing**

Sales and marketing expense increased to \$47,637 and \$81,376 for the three and six month period ended June 30, 2012 compare to \$27,439 and \$53,925 for the same period of 2011, representing an increase of 73.6% and 50.9%. The increases are result of increases in travel and entertainment expense being incurred during the periods in 2012 for brand relationship building. During the six month period ended June 30, 2012, XCXD represented \$28,687 (same period in 2011: \$15,413) or 35.3% (same period in 2011: 28.5%) of the sales and marketing expenses.

## **General and Administrative**

General and administrative expense increased to \$247,592 and \$461,842 for the three and six month period ended June 30, 2012 compared to \$183,613 and decreased to \$357,765 for the same periods of 2011, representing increases of 34.8% and 29.1% respectively. During the six month period ended June 30, 2012, XCXD represented \$265,634 (same period in 2011: \$162,739) or 57.5% (same period in 2011: 45.5%) of the general and administrative expenses. The increase is mainly due to expansion of operation into other product sectors that include consultancy fee in different aspects, renting of offsite warehouse and setting up a branch office in Hangzhou.

## **Salaries and Benefits**

Salaries and benefits expense increased to \$463,042 and \$907,705 for the three and six month period ended June 30, 2012 compared to \$365,852 and \$697,807 for the same period of 2011, representing an increases of 26.6% and 30%. During the six month period ended June 30, 2012, XCXD represented \$653,857 (same period in 2011: 448,347) or 72% (same period in 2011: 64.2%) of the salaries and benefits expenses. The increase is mainly attributable to potential business expansion in XCXD.

## **Share-based compensation**

The Company recorded \$22,377 and \$44,754 share-based compensation expense for the three and six month period ended June 30, 2012 compared to \$nil and \$nil for the same period of 2011. The increase is due to stock option issuance in August and December 2011 is being amortized.

## **Loss on Disposal of Assets**

During the first quarter of 2012, Shenzhen office wrote down \$2,385 of inventory. During the same period of 2011, XCXD has written off the residual value of \$1,450 of computer equipment bought in 2007.

During the second quarter of 2012, there is \$nil on disposal of assets while for the same period of time in 2011, the lease of Fireswirl Systems ended on June 30, 2011 and a loss on disposal of fixed assets of \$5,280 was recognized in respect of office furniture and equipment due to office moving.



### **Finance Income**

The Company recorded \$2,897 and \$5,615 of interest income for the three and six month period ended June 30, 2012 (same period in 2011: \$2,357 and \$4,001). This interest income is mainly earned by XCXD restricted cash deposit for the six month period ended June 30, 2012 and 2011.

### **Finance Expense**

The Company recorded \$113,582 and \$198,883 of interest expense for the three and six month period ended June 30, 2012 (same period in 2011: \$68,495 and \$132,410). This interest expense was incurred by the short term loans and long term loan drawn down by XCXD for the six month period ended June 30, 2012 and 2011. During the second quarter of 2011, XCXD has received \$22,350 (RMB150,000) from government as a government subsidy for business on interest expense for the year 2010.

### **Foreign Exchange Gain**

The Company recognized foreign exchange gain of \$475 and \$1,272 for the three and six month period ended June 30, 2012. The Company does not utilize any hedges or forward contract arrangements.

### **Net Comprehensive Loss**

The Company reported net comprehensive loss attributable to the common shares of \$204,732 and \$231,318 for the three and six month periods ended June 30, 2012 compared to net comprehensive loss attributable to the common shares of \$382,847 and \$607,936 for the same period of 2011, representing a decrease in loss of 46.5% and 62%.

Diluted loss per share was \$0.00 and \$0.01 for the three and six month period ended June 30, 2012 compared to a diluted loss of \$0.01 and \$0.02 in the same period of 2011.

### **Non Controlling Interest**

The Company's foreign subsidiary, XCXD realized the net income of \$29,125 and net loss of \$55,231 for the three and six month period ended June 30, 2012 compared to the same period in 2011 with net loss at \$186,930 and \$373,861, a decrease of 115.6% and 70.1% respectively. Based on the Company's ownership of 50%, only 50% of the net income/loss is being taken out/added to in the interim condensed consolidated income statement.

## **CASH FLOW STATEMENT**

### **Operating Activities**

Cash by operating activities was an inflow of \$905,943 and outflow of \$314,890 for the three and six month period ended June 30, 2012 compared to cash inflow to operation of \$1,112,776 and outflow of \$795,424 for the same period of 2011, representing 18.6% and 60.4% decrease in cash inflow and outflow respectively. The increase in cash inflow for the six month period is mainly due to decrease in accounts payable and deposits and inventory and increase in accounts receivable.

## **Investing Activities**

Cash used by investing activities was \$3,465 and \$27,289 for the three and six month period ended June 30, 2012 compared to \$8,647 and \$136,757 for the same period of 2011 representing a decrease of 59.9% and 80%. The company's investing activities in the six months of 2011 consisted mainly of acquisition of capital assets by XCXD in 2011 Q1.

## **Financing Activities**

Cash inflow from financing activities was \$81,873 and \$917,098 for the three and six month period ended June 30, 2012 compared to \$645,554 and \$2,325,705 cash inflow for the same period of 2011. The cash inflow for the 6 month period ended June 30, 2012 is mainly from the short term loan drawn down and proceeds from exercising of warrants which expired on April 28, 2012 and exercising of stock option. The cash outflow at the same period of time is the cash used for repaying of long term loan.

## **LIQUIDITY AND CAPITAL RESOURCES**

As at June 30, 2012, the Company has \$nil of long term debt, \$227,600 in cash and short term investments and working capital (defined as current assets less current liabilities) of \$671,904 compared to \$nil of long term debt, \$75,677 in cash and short term investments and working capital of \$1,005,472 as at December 31, 2011. Recent dramatic change in the global economic environment has resulted in increased uncertainty regarding future revenue and customer commitments, both in terms of timing and magnitude for such future sales. Contractual commitments are summarized in "Contractual Obligations" section of this MD&A. To the extent the Company is unable to cover its ongoing cash requirements through operations, the Company expects to raise additional equity financing to cover any shortfall. There can be no assurance that such financing and profitability will occur in the amounts and with terms expected. These condensed consolidated interim financial statements do not give effect to adjustments that would be necessary to the carrying value and classification of assets and liabilities should the Company be unable to continue as a going concern.

The Company does not have commitments for capital expenditures as of June 30, 2012. The Company's capital resources consist of common share issuances.

### **Contractual Obligations**

The Company signed a three year lease agreement for an office space in Vancouver on May 1, 2012, which will expire on April 30, 2015.

The Company's future minimum annual payments under operating leases are the following:

2012	\$ 90,579
2013	\$165,441
2014	\$ 42,602
2015	\$ 14,320

### **Related Party Transactions**

During the six months of 2012, the Company paid \$36,000 (same period in 2011: \$31,500) in professional fee to one of its officers as Interim CFO remuneration and paid \$8,000 (same period in 2011:

\$4,400) to directors as director fees. As of June 30, 2012, the accounts payable balance includes \$67,419 (same period 2011: \$12,240) that is incurred from regular operational expenses outstanding to an officer of the company and the Company also had a balance of \$597,325 (same period in 2011: \$506,449) due to the shareholders of Fireswirl and XCXD.

All of the above transactions were in the normal course of operations and are measured and recorded at the exchange amount of consideration established and agreed to by the related parties.

## **SIGNIFICANT ACCOUNTING POLICIES**

Significant accounting policies and methods used in preparation of the Company's financial statements are described in Note 2 of interim condensed consolidated financial statements of the Company for the three and six month period ended June 30, 2012.

## **CHANGES IN ACCOUNTING POLICIES**

The Company has prepared its June 30, 2012 interim condensed consolidated financial statements in accordance with IFRS 1, First-time Adoption of International Financial Reporting Standards, and with IAS 34, Interim Financial Reporting, as issued by the IASB. Previously the Company prepared its financial statements in accordance with Canadian GAAP.

The Company's IFRS accounting policies are provided in note 2 to the interim condensed consolidated financial statements. The adoption of IFRS did not result in material differences between the statement of cash flows presented under IFRSs and the statement of cash flows presented under previous Canadian GAAP and thus the statements of cash flows have not been restated in accordance with IFRS.

The transition to IFRS has resulted in a number of changes to the presentation of our financial statements to the consolidated balance sheet and the consolidated statement of operations.

The company grants stock options to certain directors and certain employees of the Company as an element of compensation. In accordance with Canadian GAAP, the grant date fair value of such options is recognized as compensation expense over the related service period with a corresponding increase in contributed surplus.

In accordance with IFRS, contributed surplus does not arise as a result of the granting of stock options. Accordingly, contributed surplus related to stock options has been reclassified to "Share-based payments reserve" which is a separate component of equity.

Additionally, under IFRS, non-controlling interest in the consolidated balance sheet is classified as equity and is presented separately from equity attributable to equity holders of the Company.

Previously, Canadian GAAP did not provide the same level of specificity of expense analysis. IFRS-IASB requires that expenses be presented using either a nature approach or a function approach; the Company has selected the nature approach.

The above changes are reclassifications within our balance sheets and statements of operations so there is no net impact to our profit as a result of these changes.

## **Other exemptions**

Other significant IFRS 1 exemptions taken by the Company as at January 1, 2010 include the following:

- Business combinations entered into prior to January, 2010 were not retrospectively restated in accordance with IFRS. Accordingly, any goodwill arising on such business combinations before the January 1, 2010 transition has not been adjusted from the carrying value previously determined under Canadian GAAP as a result of applying these exemptions.
- Currency translation differences – in accordance with IFRS transitional provisions, the Company has elected to reset the cumulative translation adjustment account, which includes gains and losses arising from the translation of foreign operations, to zero at the Transition Date. In the absence of this transitional provision, retrospective application of IFRS would require the company to determine cumulative translation differences in accordance with IAS 21, The Effects of Changes in Foreign Exchange Rates from the date a subsidiary was formed or acquired.
- Borrowing costs – IFRS 1 permits an entity to use the prospective transitional provisions in IAS 23, Borrowing Costs, for prospective application, with an effective date being the later of January 1, 2009 or the transition date. The Company has elected prospective application as of the Transition Date.

## **CRITICAL ACCOUNTING ESTIMATES**

There are a number of accounting estimates underlying the accounting policies the Company applies in preparing its financial statements. The following are those which management has determined to be material.

### **Revenue Recognition**

The Company generates its revenue from online merchandize resale, online advertising, system setup fees, customization fees, service and licensing fees.

Revenue from the sale of online merchandize is recognized in our accounts when title and risk passes to the buyer, collection is reasonably assured and the price is reasonably determinable.

System setup fees and customization fees are recognized at the time when service is delivered, following agreement of fees and contractual arrangements and when collection of amounts due is considered to be reasonably assured.

Advertising and service fees are recognized when the service is performed, there are no significant obligations remaining, the sales price is determinable and collectability is reasonably assured.

Licensing fees are recognized ratably over the period of the licensing term, once the service is delivered, following agreement of fees and contractual arrangements and when the collection of amounts due is considered to be reasonably assured. Cash received in excess of the revenue recognized is deferred.

### **Allowance for Doubtful Accounts**

The Company charges license fees to licensees based on their level of activity. The Company's management exercises judgment in making collectability assumptions on a customer by customer basis in determining whether receivables are collectible and in determining the appropriate allowance for doubtful accounts based on knowledge of the customer's payment history and expectation of collectability.

### **Intangible Assets**

The Company estimates future cash flows attributable to intangible assets for purposes of the evaluation of potential impairment based on its expectations of future market conditions. These estimates require the use of forward-looking assumptions based on past experience as well as future expectation arising from the Company's strategic and financial planning activities. Changes to these assumptions and future market conditions could result in changes to the impairment and recoverability assumption for these assets.

### **RISKS AND UNCERTAINTIES**

Important risks factors that could cause actual results, performance or achievements to be materially different than past performance or those implied by forward looking statements include:

- Foreign currency exchange risk
- Uncertainty as to the degree of new and continuing market acceptance of our products
- Our products could contain defects that lead to costs, damage of reputation or litigation
- Our dependence on brand partners' performance
- Uncertainty regarding future profitability
- Uncertainty regarding the pricing, reporting and collection of accounts
- Risks associated with sales in foreign countries and their government policy and regulations therein
- Our ability to attract and retain key personnel

### **Subsequent Events**

There is no subsequent event.

### **Off Balance Sheet Arrangement**

As at June 30, 2012 and the date of this report the Company has not entered into any off balance sheet arrangements.

### **Financial Instruments and Other Instruments**

The Company's financial instruments consists of cash, short term investments, accounts receivable, accounts payable and accrued liabilities, income taxes recovery and capital lease obligations. The fair values of these financial instruments approximate their carrying values, except as noted below. It is management's opinion that the Company is not exposed to significant interest risks. The Company's short term investments consist of investments in low risk bank certificates. A substantial portion of the Company's revenue is earned in foreign currencies and is exposed to currency fluctuations. The Company does not use financial derivatives or "other financial instruments".

## **INTERNAL CONTROL OVER FINANCIAL REPORTING AND DISCLOSURE CONTROLS**

The Company evaluated the effectiveness and design of its disclosure controls and procedures for the period ended June 30, 2012 and based on this evaluation (which included testing of the key controls by examining evidence demonstrating their existence on a test basis) have determined these controls to be effective.

The Company's financial reporting procedures and practices have enabled the certification of Fireswirl Technologies Inc. annual filing in compliance with Multilateral Instrument 52-109 "Certification of Disclosure in Issuers Annual and Interim Filings". Management has designed such internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements and other annual filings in accordance with Canadian Generally Accepted Accounting Principles, except as noted below.

Given the size of the Company, the evaluation of the design of internal controls over financial reporting for the Company resulted in the identification of the following weaknesses:

Management is aware that due to its relatively small scale of operation there is a lack of segregation of duties to a limited number of employees dealing with accounting and financial matters. However, management has concluded that considering the employees involved and the control procedures in place, including management and Audit Committee oversight, risks associated with such lack of segregation of duties are not significant enough to justify the expense associated with adding employees to segregate duties.

Management is aware that in-house expertise to deal with complex taxation, accounting and reporting issues may not be sufficient. The Company requires outside assistance and advice on new accounting pronouncements and complex accounting and reporting issues, which is common with companies of similar size.

There have been no significant changes to the Company's internal control over financial reporting that occurred during the most recent period that have materially affected, or are reasonable likely to materially affect, the Company's internal control over financial reporting. The Company internal control systems continue to evolve as the Company grows. We believe these systems are sufficient to execute the business plan and provide meaningful information upon which to manage the business. Management believes the disclosure, controls and procedures currently in place are effective.

## **OUTSTANDING SHARE DATA**

The Company has 45,571,285 common shares and 2,240,000 options outstanding at June 30, 2012 and at the date of this MD&A. If all of the Company's outstanding and exercisable options were exercised, the Company would have 47,111,285 common shares outstanding at the date of this MD&A.