

**Consolidated Financial Statements of**

***FIRESWIRL TECHNOLOGIES INC.***

**Six months ended June 30, 2012 and 2011**

**(Unaudited)**

# **FIRESWIRL TECHNOLOGIES INC.**

## **Consolidated Statement of Financial Position Unaudited (Expressed in Canadian Dollars)**

|  | Note | June 30,<br>2012    | December 31,<br>2011 |
|--|------|---------------------|----------------------|
| <b>ASSETS</b>  |      |                     |                      |
| Current assets   |      |                     |                      |
| Cash and cash equivalents                              |      | \$ 227,600          | \$ 75,677            |
| Restricted cash  | 4    | 1,924,800           | 1,698,800            |
| Amounts receivable                                     | 5    | 1,470,327           | 1,141,874            |
| GST/VAT recoverable                                    |      | -                   | 24,528               |
| Deposits and prepayments                               |      | 1,019,714           | 1,698,814            |
| Inventory  | 6    | 3,207,413           | 2,874,465            |
|  |      | 7,849,854           | 7,512,158            |
| Capital assets   |      |                     |                      |
| Trademark  | 7    | 259,348             | 308,311              |
| Goodwill   | 8    | 19,176              | 19,176               |
|  |      | 306,926             | 306,926              |
| <b>TOTAL ASSETS</b>                                    |      | <b>\$ 8,435,304</b> | <b>\$ 8,146,571</b>  |
| <b>LIABILITIES</b>                                     |      |                     |                      |
| Current liabilities                                    |      |                     |                      |
| Accounts payable and accrued liabilities               | 10   | 1,249,403           | 937,731              |
| Taxes payable  |      | 15,199              | 37                   |
| Loan from shareholders                                 | 16   | 597,377             | 997,545              |
| Short term loan  | 11   | 5,315,971           | 4,552,714            |
| Current portion of long term loan                      | 12   | -                   | 18,659               |
| Total Current Liabilities                              |      | 7,177,950           | 6,506,686            |
| Long Term Loan   | 12   | -                   | -                    |
| <b>TOTAL LIABILITIES</b>                               |      | <b>7,177,950</b>    | <b>6,506,686</b>     |
| <b>SHAREHOLDERS' EQUITY</b>                            |      |                     |                      |
| Common shares  | 13   | 7,015,340           | 6,695,007            |
| Share-based payments reserve - warrants                | 13   | 2,606,979           | 2,752,081            |
| Share-based payments reserve - options                 | 13   | 780,972             | 738,948              |
| Accumulated Other Comprehensive Income/(Loss)          | 1    | 124,865             | 223,382              |
| Accumulated Deficit                                    | 1    | (9,606,671)         | (9,160,633)          |
| Total equity attributable to equity holders of company |      | 921,485             | 1,248,785            |
| Non-controlling interest                               | 9    | 335,868             | 391,100              |
| <b>TOTAL EQUITY</b>                                    |      | <b>1,257,353</b>    | <b>1,639,885</b>     |
| Total Liabilities and Shareholders' Equity             |      | \$ 8,435,304        | \$ 8,146,571         |

See accompanying notes to the condensed consolidated financial statements.

Nature and continuance of operations (Note 1)

Commitments and contingencies (Note 17)

Subsequent events (Note 20)

On behalf of the Board:

**"Tony Lau"**

**"Ji Yoon"**

## **FIRESWIRL TECHNOLOGIES INC.**

### **Consolidated Statement of Comprehensive Income Unaudited (Expressed in Canadian Dollars)**

|  | Note  | Three months end |                  | Six months end   |                  |
|--|-------|------------------|------------------|------------------|------------------|
|  |       | June 30,<br>2012 | June 30,<br>2011 | June 30,<br>2012 | June 30,<br>2011 |
| <b>Operating revenues</b>                    |       |                  |                  |                  |                  |
| Sales revenue                                |       | 5,452,645        | 4,903,963        | 8,748,977        | 9,063,174        |
| Advertising revenue                          |       | -                | -                | -                | -                |
| Service revenue                              |       | 377,533          | 98,012           | 569,042          | 115,773          |
|  | 3     | 5,830,178        | 5,001,975        | 9,318,019        | 9,178,947        |
| Other operating income/(loss)                |       | -                | -                | -                | -                |
| <b>Total operating income</b>                |       | <b>5,830,178</b> | <b>5,001,975</b> | <b>9,318,019</b> | <b>9,178,947</b> |
| <b>Operating expenses</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          | 142,894          |
| Foreign Exchange (gain)/loss                 |       | 475              | -                | 1,272            | -                |
| Depreciation and amortization                | 7     | 40,333           | 42,915           | 80,493           | 81,730           |
| Sales and marketing                          |       | 47,637           | 27,439           | 81,376           | 53,925           |
| General administration                       |       | 247,592          | 183,613          | 461,842          | 357,765          |
| Salaries and benefits                        |       | 463,042          | 365,852          | 907,705          | 697,807          |
| Share-based compensation                     |       | 22,377           | -                | 44,754           | -                |
| Loss on disposal of assets                   |       | -                | 5,280            | 2,385            | 6,730            |
| Bad debt expense                             |       | -                | -                | -                | -                |
| <b>Total operating expense</b>               |       | <b>5,891,080</b> | <b>5,534,519</b> | <b>9,520,852</b> | <b>9,841,298</b> |
| Operating income/(loss)                      |       | (60,902)         | (532,544)        | (202,833)        | (662,351)        |
| Finance income                               |       | 2,897            | 2,357            | 5,615            | 4,001            |
| Finance costs                                | 11,12 | (113,582)        | (68,495)         | (198,883)        | (132,410)        |
| <b>Income/(Loss) before income tax</b>       |       | <b>(171,587)</b> | <b>(598,682)</b> | <b>(396,101)</b> | <b>(790,760)</b> |
| Income tax recovery (expenses)               |       | (15,313)         | -                | (15,313)         | (4,551)          |
| <b>Net income/(loss)</b>                     |       | <b>(186,900)</b> | <b>(598,682)</b> | <b>(411,414)</b> | <b>(795,311)</b> |
| Other comprehensive income/(loss)            |       |                  |                  |                  |                  |
| Foreign exchange currency adjustment         |       | 11,294           | 28,905           | 124,865          | 2,712            |
| <b>Net comprehensive income/(loss)</b>       |       | <b>(175,606)</b> | <b>(569,777)</b> | <b>(286,549)</b> | <b>(792,599)</b> |
| Net income/(loss) attribute to:              |       |                  |                  |                  |                  |
| Common shares                                |       | (218,273)        | (411,752)        | (446,037)        | (610,648)        |
| Non-controlling interest                     | 9     | 31,373           | (186,930)        | 34,623           | (184,663)        |
|  |       | (186,900)        | (598,682)        | (411,414)        | (795,311)        |
| Comprehensive income/(loss) attributable to: |       |                  |                  |                  |                  |
| Common shares                                |       | (204,731)        | (382,847)        | (231,318)        | (607,936)        |
| Non-controlling interest                     | 9     | 29,125           | (186,930)        | (55,231)         | (184,663)        |
|  |       | (175,606)        | (569,777)        | (286,549)        | (792,599)        |
| Net income/(loss) per common share           |       |                  |                  |                  |                  |
| Basic  |       | (0.00)           | (0.01)           | (0.01)           | (0.02)           |
| Diluted                                      |       | (0.00)           | (0.01)           | (0.01)           | (0.02)           |
| Comprehensive income/(loss) per common share |       |                  |                  |                  |                  |
| Basic  |       | (0.00)           | (0.01)           | (0.01)           | (0.02)           |
| Diluted                                      |       | (0.00)           | (0.01)           | (0.01)           | (0.02)           |

See accompanying notes to the condensed consolidated financial statements.

# FIRESWIRL TECHNOLOGIES INC.

## Consolidated Statement of Changes in Equity Unaudited (Expressed in Canadian Dollars)

|   | Number of shares  | Share capital       | Contributed Surplus - Warrants | Contributed Surplus - Options | Other Comprehensive Income | Accumulated deficit   | Total             | Non-controlling interest | Total equity        |
|---|-------------------|---------------------|--------------------------------|-------------------------------|----------------------------|-----------------------|-------------------|--------------------------|---------------------|
| Balance, January 1, 2010                      | 31,361,285        | \$ 5,610,417        | \$ 2,606,979                   | \$ 724,419                    | \$ -                       | \$ (7,133,999)        | \$ 1,807,816      | \$ 502,492               | \$ 2,310,309        |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (933,977)             | (933,977)         | 11,565                   | (922,412)           |
| Compensation expense related to Stock Options |                   |                     |                                | 7,054                         |                            |                       | 7,054             |                          | 7,054               |
| Issuance of shares                            | 7,000,000         | 350,000             |                                |                               |                            |                       | 350,000           |                          | 350,000             |
| Share issuance costs                          |                   | (5,152)             |                                |                               |                            |                       | (5,152)           |                          | (5,152)             |
| Foreign currency translation difference       |                   |                     |                                |                               | 42,279                     |                       | 42,279            |                          | 42,279              |
| <b>Balance at December 31, 2010</b>           | <b>38,361,285</b> | <b>5,955,265</b>    | <b>2,606,979</b>               | <b>731,474</b>                | <b>42,279</b>              | <b>(8,067,976)</b>    | <b>1,268,021</b>  | <b>514,057</b>           | <b>1,782,077</b>    |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (230,097)             | (230,097)         | 7,275                    | (222,823)           |
| Option exercised                              | 50,000            | 4,500               |                                | (2,000)                       |                            |                       | 2,500             |                          | 2,500               |
| Foreign currency translation difference       |                   |                     |                                |                               | (21,186)                   |                       | (21,186)          | (5,008)                  | (26,193)            |
| <b>Balance at March 31, 2011</b>              | <b>38,411,285</b> | <b>5,959,765</b>    | <b>2,606,979</b>               | <b>729,474</b>                | <b>21,093</b>              | <b>(8,298,073)</b>    | <b>1,019,238</b>  | <b>516,324</b>           | <b>1,535,561</b>    |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (374,450)             | (374,450)         | (195,326)                | (569,776)           |
| Option exercised                              | 130,000           | 18,700              |                                | (5,201)                       |                            |                       | 13,500            |                          | 13,500              |
| Option expired                                |                   | 67,460              |                                | (67,460)                      |                            |                       |                   |                          |                     |
| Issuance of shares                            | 6,100,000         | 650,953             | 145,102                        |                               |                            |                       | 796,055           |                          | 796,055             |
| Share issuance costs                          |                   | (22,871)            |                                |                               |                            |                       | (22,871)          |                          | (22,871)            |
| Foreign currency translation difference       |                   |                     |                                |                               | 20,509                     |                       | 20,509            | 8,396                    | 28,905              |
| <b>Balance at June 30, 2011</b>               | <b>44,641,285</b> | <b>6,674,007</b>    | <b>2,752,081</b>               | <b>656,813</b>                | <b>41,603</b>              | <b>(8,672,523)</b>    | <b>1,451,981</b>  | <b>329,393</b>           | <b>1,781,374</b>    |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (488,110)             | (488,110)         | (35,529)                 | (523,639)           |
| Compensation expense related to Stock Options |                   |                     |                                | 103,135                       |                            |                       | 103,135           |                          | 103,135             |
| Option expired                                |                   | 21,000              |                                | (21,000)                      |                            |                       |                   |                          |                     |
| Foreign currency translation difference       |                   |                     |                                |                               | 181,779                    |                       | 181,779           | 97,235                   | 279,015             |
| <b>Balance at December 31, 2011</b>           | <b>44,641,285</b> | <b>6,695,007</b>    | <b>2,752,081</b>               | <b>738,948</b>                | <b>223,382</b>             | <b>(9,160,633)</b>    | <b>1,248,785</b>  | <b>391,100</b>           | <b>1,639,885</b>    |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (227,765)             | (227,765)         | 3,250                    | (224,514)           |
| Compensation expense related to Stock Options |                   |                     |                                | 22,377                        |                            |                       | 22,377            |                          | 22,377              |
| Warrants exercised                            | 50,000            | 11,830              | (2,329)                        |                               |                            |                       | 9,501             |                          | 9,501               |
| Option expired                                |                   | 1,530               |                                | (1,530)                       |                            |                       |                   |                          |                     |
| Foreign currency translation difference       |                   |                     |                                |                               | (109,812)                  |                       | (109,812)         | (87,607)                 | (197,419)           |
| <b>Balance at March 31, 2012</b>              | <b>44,691,285</b> | <b>\$ 6,708,367</b> | <b>\$ 2,749,752</b>            | <b>\$ 759,795</b>             | <b>\$ 113,570</b>          | <b>\$ (9,388,398)</b> | <b>\$ 943,086</b> | <b>\$ 306,743</b>        | <b>\$ 1,249,830</b> |
| Net Income/(Loss) for the period              |                   |                     |                                |                               |                            | (218,273)             | (218,273)         | 31,373                   | (186,901)           |
| Compensation expense related to Stock Options |                   |                     |                                | 22,377                        |                            |                       | 22,377            |                          | 22,377              |
| Warrants exercised                            | 850,000           | 201,087             | (39,587)                       |                               |                            |                       | 161,500           |                          | 161,500             |
| Warrants expired                              |                   | 100,132             | (100,132)                      |                               |                            |                       |                   |                          |                     |
| Option exercised                              | 30,000            | 2,700               |                                | (1,200)                       |                            |                       | 1,500             |                          | 1,500               |
| Share issuance costs (expired warrants)       |                   | 3,055               | (3,055)                        |                               |                            |                       |                   |                          |                     |
| Foreign currency translation difference       |                   |                     |                                |                               | 11,294                     |                       | 11,294            | (2,247)                  | 9,047               |
| <b>Balance at June 30, 2012</b>               | <b>45,571,285</b> | <b>\$ 7,015,340</b> | <b>\$ 2,606,979</b>            | <b>\$ 780,972</b>             | <b>\$ 124,865</b>          | <b>\$ (9,606,671)</b> | <b>\$ 921,485</b> | <b>\$ 335,869</b>        | <b>\$ 1,257,353</b> |

See accompanying notes to the consolidated financial statements.

## **FIRESWIRL TECHNOLOGIES INC.**

### **Consolidated Statements of Cash Flows Unaudited (Expressed in Canadian Dollars)**

|   | Three months end |                  | Six months end   |                  |
|---|------------------|------------------|------------------|------------------|
|   | June 30,<br>2012 | June 30,<br>2011 | June 30,<br>2012 | June 30,<br>2011 |
| <b>OPERATING ACTIVITIES</b>                               |                  |                  |                  |                  |
| Net income/(loss) for the period                          | \$ (186,900)     | \$ (598,682)     | \$ (411,414)     | \$ (795,311)     |
| Non cash items:   |                  |                  |                  |                  |
| Depreciation and amortization                             | 40,333           | 42,915           | 80,493           | 81,730           |
| Share-based compensation                                  | 22,377           | -                | 44,754           | -                |
| Loss on fixed assets disposal                             | -                | 5,280            | 2,385            | 6,730            |
| Changes in non-cash working capital items:                |                  |                  |                  |                  |
| Amounts receivable  | (641,719)        | (523,953)        | (303,925)        | (556,846)        |
| Deposits and prepayments                                  | 590,711          | 1,132,645        | 679,099          | 20,737           |
| Inventory   | 1,047,663        | 112,056          | (332,947)        | (219,899)        |
| Accounts payable and accrued liabilities                  | 151,127          | 720,190          | 311,673          | 548,394          |
| Loan from shareholders                                    | (132,848)        | 226,788          | (400,168)        | 119,041          |
| Income taxes payable                                      | 15,199           | (4,542)          | 15,162           | -                |
|   | 905,943          | 1,112,697        | (314,889)        | (795,424)        |
| <b>INVESTING ACTIVITIES</b>                               |                  |                  |                  |                  |
| Deferred development costs and other asset                | -                | -                | -                | -                |
| Acquisition of capital assets                             | (3,465)          | (10,447)         | (27,289)         | (138,557)        |
| Proceeds from sales of capital assets                     | -                | 1,800            | -                | 1,800            |
|   | (3,465)          | (8,647)          | (27,289)         | (136,757)        |
| <b>FINANCING ACTIVITIES</b>                               |                  |                  |                  |                  |
| Proceeds/(Repayment) of short term loan                   | (76,429)         | (125,086)        | 763,257          | 1,562,983        |
| Repayment of long-term loan                               | (4,698)          | (10,889)         | (18,659)         | (21,307)         |
| Shares issued for cash                                    |                  | 768,030          |                  | 768,030          |
| Shares issued for warrants/options exercised              | 163,000          | 13,500           | 172,500          | 16,000           |
|   | 81,873           | 645,555          | 917,098          | 2,325,706        |
| Increase/(Decrease) in cash during the period             | 984,351          | 1,749,605        | 574,920          | 1,393,525        |
| Effect of foreign exchange                                | 2,448            | 34,001           | (194,997)        | (24,708)         |
| Cash and cash equivalents, beginning of period            | 1,165,601        | 731,070          | 1,772,477        | 1,145,859        |
| Cash and cash equivalents, end of period                  | \$ 2,152,400     | \$ 2,514,676     | \$ 2,152,400     | \$ 2,514,676     |
| <b>Supplemental disclosure with respect to cash flows</b> |                  |                  |                  |                  |
| Cash paid for:  |                  |                  |                  |                  |
| Interest  | \$ 113,582       | 90,932           | \$ 198,883       | 132,410          |
| Income taxes  | \$ -             | 33,453           | \$ -             | 58,627           |

See accompanying notes to the consolidated financial statements.

**FIRESWIRL TECHNOLOGIES INC.**  
**Notes to the Interim Condensed Consolidated Financial Statements**  
**For the period ended June 30, 2012 and 2011**  
**(Unaudited)**

**Note 1- Nature and Continuance of Operations**

Fireswirl Technologies Inc. ("the Company") was founded in 1999 and became publicly listed in 2006. The address of the Company's registered office is Suite 2823, Three Bentall Centre, 595 Burrard Street, Vancouver, British Columbia. The Company focuses on technology development and deployment, and conducting e-commerce, including operating official online stores for international brands in China and reselling branded products on these online stores.

These financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. If the going concern assumption were not appropriate for these financial statements then adjustments would be necessary in the carrying value of assets and liabilities, the reported revenue and expenses and the balance sheet classifications used.

Several adverse conditions cast doubt on the validity of this assumption. During the three month period ended June 30, 2012 and 2011, the Company experienced operating losses and negative operating cash flows which were primarily funded by borrowing of short term loans.

The continuing operations of the Company are dependent upon its ability to continue to raise adequate financing, and to commence profitable operations in the future. There is no assurance the Company will be able to achieve profitable operations or continue raising funds in the future.

|                 | June 30, 2012  | December 31, 2011 | June 30, 2011  |
|-----------------|----------------|-------------------|----------------|
| Deficit         | \$ (9,606,671) | \$ (9,160,633)    | \$ (8,592,126) |
| Working Capital | 671,904        | 1,005,472         | 1,083,670      |

**Note 2 - Significant Accounting Policies**

The accounting policies set out below have been applied consistently to all periods presented in these condensed consolidated interim financial statements. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

**a) Statement of Compliance**

These condensed consolidated interim financial statements of the Corporation have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB"). The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements.

The condensed consolidated interim financial statements were authorized for issue by the Board of Directors on August 22, 2012.

**b) Basis of Presentation**

The condensed consolidated interim financial statements have been prepared mainly under the historical cost convention. Other measurement bases used are described in the applicable notes.

**FIRESWIRL TECHNOLOGIES INC.**  
**Notes to the Interim Condensed Consolidated Financial Statements**  
**For the period ended June 30, 2012 and 2011**  
**(Unaudited)**

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The Company's financial year corresponds to the calendar year. The consolidated financial statements are prepared in Canadian dollars.

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries as follows:

- acquisition cost is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, excluding transaction costs which are expensed as incurred;
- identifiable assets acquired and liabilities assumed are measured at their fair values at the acquisition date;
- the excess of acquisition cost over the fair value of the identifiable net assets acquired is recorded as goodwill;
- if the acquisition cost is less than the fair value of the net assets acquired, the fair value of the net assets is re-assessed and any remaining difference is recognized directly in the income statement;
- contingent consideration is measured at fair value on the acquisition date, with subsequent changes in the fair value recorded through the income statement when the contingent consideration is a financial liability. Contingent consideration is not re-measured when it is an equity instrument; and
- upon gaining control in a step acquisition, the existing ownership interest is re-measured to fair value through the income statement.

Associates are those entities where the Company has the ability to exercise significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Company holds between 20 and 50 percent of the voting power of an entity. Joint ventures are those entities over whose activities the Company has joint control, established by contractual agreement and requiring unanimous consent for strategic financial and operating decisions.

Associates and jointly controlled entities are accounted for using the equity method (equity accounted investees) and are generally recognized initially at cost. The consolidated financial statements include the Company's share of income and expenses and equity movements of equity accounted investees, after adjustments to align the accounting policies with those of the Company, from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. When the Company's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the Company has an obligation or has made payments on behalf of the investee.

These condensed consolidated interim financial statements include the accounts of the Company and its subsidiaries and associates as follows:

**FIRESWIRL TECHNOLOGIES INC.**  
**Notes to the Interim Condensed Consolidated Financial Statements**  
**For the period ended June 30, 2012 and 2011**  
**(Unaudited)**

| Name  | Place of incorporation               | Ownership |
|---|--------------------------------------|-----------|
| Fireswirl Systems Inc.                                  | Province of British Columbia, Canada | 100%      |
| Fireswirl Asia Ltd.                                     | Hong Kong, China                     | 100%      |
| Fireswirl Mobile Solutions Ltd.                         | Hong Kong, China                     | 100%      |
| M- Lingo Limited  | British Virgin Island                | 51%       |
| SMS Translators Limited                                 | British Virgin Island                | 51%       |
| Fireswirl Technologies (Shenzhen) Co.Ltd.               | Shenzhen, China                      | 100%      |
| Fireswirl Technologies (Beijing) Co. Ltd.               | Beijing, China                       | 100%      |
| Beijing Xingchang Xinda Technology Development Co., Ltd | Beijing, China                       | 50%       |
| Tysen Xieli Technology Co. Ltd.                         | Beijing, China                       | 21%       |

In 2009, Tsyen Xieli Technology is an investment over which the Company is able to exercise significant influence and is accounted for by the equity method. This investment has been written down at the end of 2009.

All significant inter-company transactions and balances have been eliminated upon consolidation.

**c) Cash and cash equivalents**

Cash consists of cash, funds in bank accounts, and marketable securities such as guaranteed investment certificates. Interest income earned on these marketable securities is recorded on an accrual basis.

Cash is held in Canadian dollars, US dollars, Hong Kong dollars, and Chinese RMB which is not freely convertible into other currencies. Under China's Foreign Exchange Control Regulations and Administration of Settlement, Sales and Payment of Foreign Exchange Regulations, the Company is permitted to exchange RMB for other currencies through a government bank authorized to conduct foreign exchange business if the purpose of such exchange fulfills the relevant requirements.

**d) Capital assets**

Capital assets are recorded at cost and are depreciated annually on straight-line basis. Depreciation is charged using the following assumptions:

|                        |  |
|------------------------|--|
| Computer hardware      | 3 year straight-line                     |
| Furniture and fixtures | 5 year straight-line                     |
| Leasehold improvements | Straight-line over the term of the lease |

Capital assets are written down to the net recoverable value when management determines there has been a change in circumstances which indicates its carrying amount may not be recoverable.

**e) Comprehensive income**

This section establishes standards for reporting and presentation of comprehensive income, which is comprised of net earnings or loss and other comprehensive income. Comprehensive income is the change in the Company's net assets that results from transactions, events and circumstances from sources other than the Company's shareholders and includes items that would not normally



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be included in net earnings such as unrealized gains or losses on available-for-sale investments. Other comprehensive income includes the holding gains and losses from available-for-sale securities, which are not included in net income (loss) until realized.

**f) Foreign currency translation**

The Company uses the Canadian dollar as its presentation currency.

Revenue and expense transactions that are denominated in foreign currencies and entered into directly by the Company are translated into Canadian dollars at the exchange rates prevailing at the time of the transactions. Amounts receivable and payable in foreign currencies are stated in Canadian dollars at the rates of exchange prevailing at the balance sheet dates, and the resulting foreign exchange gains and losses are recognized in the net income (loss) for the year.

For consolidation purposes, the assets and liabilities of subsidiary entities whose functional currencies differ from that of the Company are translated at the exchange rate prevailing at the balance sheet date. Income statements of such entities are translated at average rates of exchange during the year. All resulting exchange differences, including exchange differences arising from the translation of borrowings and other financial instruments are recognized directly in accumulated other comprehensive income (loss).

Should a foreign operation be sold, the cumulative exchange differences recognized in accumulated other comprehensive income (loss) since January 1, 2010 would be recognized in the income statement as part of the profit or loss on sale.

**g) Income taxes**

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences:

- (i) the initial recognition of assets or liabilities in transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- (ii) differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future; and
- (iii) taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

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A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit to be realized.

**h) 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.

**i) Inventory**

Inventories are valued at the lower of cost or net realizable value. Cost is determined on a first-in, first-out basis. Inventory consists of finished goods. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. In establishing any impairment of inventory, management estimates the likelihood that inventory carrying values will be affected by changes in market demand which would impair the value of inventory on hand.

**j) Use of estimates**

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the balance sheets as well as the reported amounts of revenues, expenses, and cash flows during the periods presented. Such estimates relate primarily to unsettled transactions and events as of the date of the financial statements. Actual results could differ materially from estimated amounts.

Amounts recorded for amortization are based on the estimated lives of property, plant and equipment. Stock-based compensation is based upon expected volatility and option life estimates. The provision for income taxes is based on judgments in applying income tax law and estimates on the timing, likelihood and reversal of temporary differences between the accounting and tax basis of assets and liabilities. Valuation of the accounts receivable are based on assumptions regarding collectability. Valuation of goodwill is based on assumptions regarding recoverability of

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the recorded amount. These estimates are subject to measurement uncertainty and changes in these estimates could materially impact the financial statements of future periods.

**k) Share-based compensation plans**

The Company offers stock-based compensation to key employees and non-executive directors as described below. The Company accounts for the performance of the stock option plan, which calls for settlement by the issuance of equity instruments, using the fair value method. Under the fair value method, compensation cost attributed to the options to employees is measured at fair value at the grant date and amortized over the vesting period. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting period.

Compensation cost is recognized so that each tranche in an award with graded vesting is considered a separate grant with a different vesting date and fair value. No compensation cost is recognized for options that employees forfeit if they fail to satisfy the service requirement for vesting. Share-based payment expense relating to cash-settled awards, including share appreciation rights is accrued at the fair value of the liability. Until the liability is settled, the Company re-measures the fair value at the end of each reporting period and at the date of settlement, with any changes in fair value recognized in profit or loss for the period.

**l) Impairment**

(i) Financial assets

Financial assets not carried at fair value through profit or loss are assessed for impairment at each reporting date by determining whether there is objective evidence that indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

(ii) Non-financial assets

The carrying amounts of the Company's non-financial assets other than inventories are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite useful lives, the recoverable amount is estimated annually.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purposes of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other groups of assets. Cash-generating units to which goodwill has been allocated reflects the lowest level at which goodwill is monitored for internal reporting purposes.

An impairment loss is recognized if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognized in net

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loss. Impairment losses recognized in respect of the cash generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit on a pro-rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined net of depreciation or amortization, if no impairment loss had been recognized.

**m) Transaction Costs**

Transaction costs, other than in respect of financial assets held for trading which are expensed as incurred, are added to the initial fair value of the acquired financial asset or financial liability. The Company has selected this method as it believes that this results in a better matching of the transaction costs with the periods benefiting from the transaction costs.

**n) Goodwill**

Goodwill is recognized as the fair value of the consideration transferred including the recognized amount of any non-controlling interest in the acquired, less the fair value of the net identifiable assets acquired and liabilities assumed, as of the acquisition date. Subsequent to initial recognition, goodwill is measured at cost less accumulated impairment losses.

Goodwill acquired through a business combination is allocated to each cash-generating unit ("CGU"), or a group of CGUs, that are expected to benefit from the related business combination. A group of CGUs represents the lowest level within the entity at which the goodwill is monitored for internal management purposes, which is not higher than an operating segment.

**o) Allowance for doubtful accounts**

The Company provides an allowance for doubtful accounts when management estimates collectability to be uncertain. Accounts receivable are continually reviewed to determine which, if any, accounts are doubtful of collection. In making the determination of the appropriate allowance amount, the Company considers current economic and industry conditions, relationships with each significant customer, overall customer credit-worthiness and historical experience. If events indicate that specific receivable balances may be impaired, further consideration is given to those balances and the allowance is adjusted accordingly. Accounts are written off when the Company's efforts to collect are unsuccessful. During the six month period ended June 30, 2012, the Company recorded an allowance for doubtful accounts of \$Nil (2011 - \$Nil).

**p) Provisions**

Provisions for legal or constructive obligations are recognized when the Company has a present legal or constructive obligation that has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

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**q) Financial instruments**

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the company classifies its financial instruments in the following categories depending on the purposes for which the instruments were acquired:

- (i) **Financial assets and liabilities at fair value through profit and loss:**  
A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the statement of operations. Gains and losses arising from changes in fair value are presented in the statement of operations within other gains and losses in the period in which they arise.

Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the balance sheet date, which is classified as non-current.

- (ii) **Loans and receivables:**  
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The company's loans and receivables are comprised of trade and other receivables, contract work-in-progress, and cash and cash equivalents, and are included in current assets due to their short-term nature. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

- (iii) **Financial liabilities at amortized cost:**  
Financial liabilities at amortized cost include trade payables and accrued liabilities, deferred revenue, and debt. Financial liabilities are initially recognized at the amount required to be paid less, when material, a discount to reduce the payables to fair value. Subsequently, financial liabilities are measured at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

- (iv) **Share capital:**  
Share capital is classified as equity. Incremental costs directly attributable to the issue of shares and share options are recognized as a deduction from equity. When

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share capital is repurchased, the amount of the consideration paid, including directly attributable costs, is recognized as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from equity. When treasury shares are subsequently reissued, the amount received is recognized as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to or from retained earnings.

**r) Trade and other receivables**

Trade and other receivables are stated at their amortized cost less impairment losses. A provision for impairment is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. Receivables with a short-term duration are not discounted.

**s) Earnings (loss) per share:**

Basic earnings (loss) per share is computed using the weighted average number of common shares outstanding during the period, adjusted for treasury shares. Diluted earnings per share is calculated using the treasury stock method. Under the treasury stock method, the dilution is calculated based upon the number of common shares issued should "in the money" options, if any, be exercised. When the effects of outstanding stock based compensation arrangements would be anti-dilutive, diluted loss per share is not calculated.

**t) Government assistance**

Government grants are recognized at fair value when there is reasonable assurance that the grant will be received and all the conditions attached to it will be complied with.

When the grant relates to an asset it is recognized in deferred income and credited to other income on a systematic basis over the useful life of the asset.

When the grant relates to income it is deducted in reporting the related expense on a systematic basis over the periods in which the related costs for which the grant is intended to compensate are incurred.

**u) Future accounting pronouncements**

The following five new Standards were issued by the IASB in May 2011, and are effective for annual periods beginning on or after January 1, 2013. Early application is permitted if all five Standards are adopted at the same time.

Consolidated Financial Statements - IFRS 10 Consolidated Financial Statements ("IFRS 10") will replace existing guidance on consolidation in IAS 27 Consolidated and Separate Financial Statements, and SIC 12 Consolidation – Special Purpose Entities. The portion of IAS 27 that deals with separate financial statements will remain. IFRS 10 changes the definition of control, such that the same consolidation criteria will apply to all entities. The revised definition focuses on the need to have both "power" and "variable returns" for control to be present. Power is the current ability to direct the activities that significantly influence returns. Variable returns can be positive, negative or

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both. IFRS 10 requires continuous assessment of control of an investee in line with any changes in facts and circumstances.

Joint Arrangements - IFRS 11 Joint Arrangements ("IFRS 11") will replace IAS 31 Interests in Joint ventures, and SIC 13 Jointly Controlled Entities – Non-monetary Contributions by Venturers. IFRS 11 defines a joint arrangement as an arrangement where two or more parties contractually agree to share control. Joint control exists only when the decisions about activities that significantly affect the returns of an arrangement require the unanimous consent of the parties sharing control. The focus is not solely on the legal structure of joint arrangements, but rather on how the rights and obligations are shared by the parties to the joint arrangement. IFRS 11 eliminates the existing policy choice of proportionate consolidation for jointly controlled entities. In addition, the Standard categorizes joint arrangements as either joint operations or joint ventures.

Disclosure of Interests in Other Entities - IFRS 12 Disclosure of Interests in Other Entities ("IFRS 12") is the new Standard for disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. Matters covered include information about the significant judgments and assumptions that any entity has made in determining whether it has control, joint control or significant influence over another entity.

Separate Financial Statements - IAS 27 Separate Financial Statements ("IAS 27") has been updated to require an entity presenting separate financial statements to account for those investments at cost or in accordance with IFRS 9 Financial Instruments. The amended IAS 27 excludes the guidance on the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent currently within the scope of the current IAS 27 Consolidated and Separate Financial Statements that is replaced by IFRS 10.

Investments in Associates and Joint Ventures - IAS 28 Investments in Associates and Joint ventures ("IAS 28") has been revised and it is to be applied by all entities that are investors with joint control of, or significant influence over, an investee. The scope of IAS 28 Investments in Associates does not include joint ventures.

IFRS 13 Fair Value Measurement ("IFRS 13") was issued by the IASB in May 2011, and is effective for annual periods beginning on or after January 1, 2013. Early application is permitted. IFRS 13 was issued to remedy the inconsistencies in the requirements for measuring fair value and for disclosing information about fair value measurement in various current IFRSs. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. an exit price. The IASB has issued an amendment to IFRS 7, Financial Instruments: Disclosures ("IFRS 7"), requiring incremental disclosures regarding transfers of financial assets. This amendment is effective for annual periods beginning on or after July 1, 2011. The Company will apply the amendment at the beginning of its 2012 financial year. The Company does not expect the implementation to have a significant impact on the Company's disclosures.

The IASB has issued a new standard, IFRS 9, Financial Instruments ("IFRS 9"), which will ultimately replace IAS 39, "Financial Instruments: Recognition and Measurement" ("IAS 39"). The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments and the issuance of IFRS 9 is part of the first phase of this project. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS 9 is based on how an entity manages its financial instruments in the

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context of its business model and the contractual cash flow characteristics of the financial assets. IFRS 9 requires a single impairment method to be used, replacing multiple impairment methods in IAS 39. For financial liabilities measured at fair value, fair value changes due to changes in an entity's credit risk are presented in other comprehensive income. IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Company does not expect the implementation to have a significant impact on the Company's results of operations, financial position and disclosures.

The IASB has issued an amendment to IAS 1, Presentation of Financial Statements ("IAS 1"), which requires entities to group items presented in other comprehensive income (OCI) on the basis of whether they might at some point be reclassified from OCI to profit or loss at a later date when specified conditions are met. By requiring items of OCI to be grouped on this basis, their potential effect on profit or loss in future periods will be clearer. This amendment is effective for annual periods beginning on or after July 1, 2012 and requires full retrospective application. The Company does not expect IAS 1 to have a material impact on the financial statements.

### **Note 3 – Revenue**

#### **Revenue**

The Company generated revenue from merchandise resale and service and maintenance fees during the six month period ended June 30, 2012.

During the six month period ended June 30, 2012, the Company recognized \$8,748,977 of revenue from the merchandise sales in China (same period in 2011: \$9,063,174). Within this amount, \$8,748,977 (same period in 2011: \$9,063,174) was generated by Beijing Xingchang Xinda Technology Development Co., Ltd. ("XCXD"), a subsidiary in China.

The Company recorded \$569,042 (same period in 2011: \$115,773) of revenue from service and maintenance fees during the six month period ended June 30, 2012. Within this amount, \$509,219 (same period in 2011: \$55,261) was made by XCXD. This revenue is mainly generated from software development and maintenance services.

### **Note 4 – Restricted Cash**

The Company's subsidiary Beijing Xingchang Xinda Technology Development Co., Ltd ("XCXD") is required to maintain a deposit of RMB 2,000,000 (equivalent to \$320,800 as of June 30, 2012 and RMB2,000,000 equivalent to \$323,200 as of December 31, 2011) with its financial institution for its short term loan account. The restricted cash earns interest at the prime rate (3.10% for savings in 2012 and 2011) and is redeemable when the loan is paid off.

The company has pledged cash, RMB10M (equivalent to \$1,604,000 as of June 30, 2012), as security deposit pledge for two counter-guarantee contracts. The first counter-guarantee contract incorporates two already-signed contracts as the basis: (1) standard bank RMB10M loan contract between XCXD and China Construction Bank - "Main Contract", and (2) standard guarantor appointment contract between XCXD and China Fortune Investment Guarantee Company (CFG) to appoint CFG as XCXD's guarantor - "Guarantor Appointment Contract". The second counter-guarantee contract incorporates two already-signed contracts as the basis: (1) standard bank RMB10M loan contract between XCXD and Communication Bank - "Main Contract", and (2) standard guarantor appointment contract between XCXD and China Fortune Investment Guarantee Company (CFG) to appoint CFG as XCXD's guarantor - "Guarantor Appointment Contract".



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In summary, XCXD will provide a counter-guarantee to CFG for CFG being the guarantor of the bank loans in order to ensure the fulfillment of the Main Contract (RMB20M loan) and the Guarantor Appointment Contracts. XCXD will pledge the collateral (RMB5M to the contract) to CFG, as a counter-guarantee for the responsibility and obligation for XCXD to fulfill the contracts.

### **Note 5 – Amounts Receivable**

|                          | <b>June 30, 2012</b> | <b>December 31, 2011</b> |
|--------------------------|----------------------|--------------------------|
| Accounts receivable      | \$ 1,469,020         | \$ 1,140,612             |
| Miscellaneous receivable | 1,307                | 1,262                    |
| Total amounts receivable | <u>\$ 1,470,327</u>  | <u>\$ 1,141,874</u>      |

### **Note 6 – Inventory**

|                | <b>June 30, 2012</b> | <b>December 31, 2011</b> |
|----------------|----------------------|--------------------------|
| Finished Goods | \$ 3,207,413         | \$ 2,874,465             |

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### Note 7 - Capital Assets

|                                 | Furniture &<br>Fixtures | Computers &<br>Office Equipment | Leasehold<br>Improvement | Total      |
|---------------------------------|-------------------------|---------------------------------|--------------------------|------------|
| <i>Asset Costs</i>              |                         |                                 |                          |            |
| Balance Dec 31, 2010            | 22,872                  | 261,788                         | 168,525                  | 453,185    |
| Foreign Exchange                | 394                     | 18,435                          | 10,251                   | 29,080     |
| Additions                       | -                       | 217,850                         | -                        | 217,850    |
| Disposals                       | (17,323)                | (151,852)                       | -                        | (169,175)  |
| Balance Dec 31, 2011            | \$ 5,943                | \$ 346,220                      | \$ 178,776               | \$ 530,940 |
| Foreign Exchange                | (110)                   | (6,316)                         | (2,874)                  | (9,301)    |
| Additions                       | -                       | 23,556                          | -                        | 23,556     |
| Disposals                       | -                       | -                               | -                        | -          |
| Balance Mar 31, 2012            | \$ 5,833                | \$ 363,460                      | \$ 175,902               | \$ 545,195 |
| Foreign Exchange                | 66                      | 4,057                           | 1,724                    | 5,848      |
| Additions                       | -                       | 3,465                           | -                        | 3,465      |
| Disposals                       | -                       | -                               | -                        | -          |
| Balance Jun 30, 2012            | \$ 5,899                | \$ 370,983                      | \$ 177,626               | \$ 554,508 |
| <i>Accumulated Depreciation</i> |                         |                                 |                          |            |
| Balance Dec 31, 2010            | 11,102                  | 103,659                         | 46,672                   | 161,433    |
| Foreign Exchange                | 145                     | 7,341                           | 1,611                    | 9,097      |
| Amortization of the period      | 2,556                   | 146,679                         | 43,562                   | 192,798    |
| Disposals                       | (10,436)                | (130,263)                       | -                        | (140,699)  |
| Balance Dec 31, 2011            | \$ 3,367                | \$ 127,417                      | \$ 91,845                | \$ 222,629 |
| Foreign Exchange                | (63)                    | (2,339)                         | (1,260)                  | (3,662)    |
| Amortization of the period      | 289                     | 25,634                          | 10,688                   | 36,612     |
| Disposals                       | -                       | -                               | -                        | -          |
| Balance Mar 31, 2012            | \$ 3,594                | \$ 150,712                      | \$ 101,273               | \$ 255,579 |
| Foreign Exchange                | 41                      | 1,686                           | 877                      | 2,604      |
| Amortization of the period      | 266                     | 25,902                          | 10,810                   | 36,978     |
| Disposals                       | -                       | -                               | -                        | -          |
| Balance Jun 30, 2012            | \$ 3,901                | \$ 178,299                      | \$ 112,960               | \$ 295,160 |
| <i>Carrying Amounts</i>         |                         |                                 |                          |            |
| At December 31, 2010            | \$ 11,770               | \$ 158,128                      | \$ 121,853               | \$ 291,752 |
| At December 31, 2011            | \$ 2,576                | \$ 218,804                      | \$ 86,931                | \$ 308,311 |
| At March 31, 2012               | \$ 2,239                | \$ 212,749                      | \$ 74,629                | \$ 289,616 |
| At June 30, 2012                | \$ 1,998                | \$ 192,684                      | \$ 64,666                | \$ 259,348 |

During the six month period ended June 30, 2012, the Company recorded depreciation of \$80,493 (same period in 2011 - \$81,730).

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### **Note 8 - Goodwill**

|   | 2012              |
|---|-------------------|
| Balance, January 1, 2008                  | \$ -              |
| Acquisition of XCXD on October 1, 2009    | 306,926           |
| Balance, December 31, 2009, 2010 and 2011 | \$ 306,926        |
| Change in Q1, 2012                        | \$ -              |
| Change in Q2, 2012                        | \$ -              |
| <b>Balance, June 30, 2012</b>             | <b>\$ 306,926</b> |

### **Note 9 – Net Income attributable to non-controlling Interest (NCI)**

|   |            |
|---|------------|
| Balance – September 30, 2009                                  | \$ -       |
| Acquisitions on October 1, 2009                               | 186,519    |
| Net income attributable to non-controlling interest - Q4 2009 | 315,973    |
| Balance – December 31, 2009                                   | 502,492    |
| Net income attributable to non-controlling interest - 2010    | 11,564     |
| Balance – December 31, 2010                                   | \$ 514,056 |
| Net income attributable to non-controlling interest - 2011    | (122,956)  |
| Balance – December 31, 2011                                   | \$ 391,100 |
| Net income attributable to non-controlling interest - Q1 2012 | (84,357)   |
| Net income attributable to non-controlling interest - Q2 2012 | 29,125     |
| Balance – June 30, 2012                                       | \$ 335,868 |

The Company's foreign subsidiary XCXD comprehensive gain of \$58,250 and comprehensive loss \$110,464 for the three month and six month period ended June 30, 2012 (net loss same period in 2011 – \$373,861 and \$369,326). Based on the Company's ownership of 50%, the remaining 50% of non controlling interest of net income \$29,125 and net loss \$55,232 (net loss 2011: \$186,930 and \$184,663) for the three month period and six month period ended June 30, 2012 was deducted from the net income.

### **Note 10 - Accounts Payable and Accrued Liabilities**

Accounts payable and accrued liabilities as of June 30, 2012 consisted of accounts payable and accrued expenses, wages and vacation payable, payroll remittances and customer deposits.

|  | June 30, 2012 | December 31, 2011 |
|--|---------------|-------------------|
| Accounts payable and accrued expenses          | \$ 1,170,935  | \$ 845,096        |
| Wages and vacation payable                     | 7,529         | 86,565            |
| Payroll remittances                            | 710           | 303               |
| Sales Tax Payable                              | 24,890        | 5,767             |
| Customer deposits                              | 45,339        |                   |
| Total accounts payable and accrued liabilities | \$ 1,249,403  | \$ 937,731        |

# **FIRESWIRL TECHNOLOGIES INC.**

## **Notes to the Interim Condensed Consolidated Financial Statements**

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### **Note 11 - Short Term Loan**

| <b>Continuity</b>           | <b>2012</b> |                  | <b>2011</b> |                  |
|-----------------------------|-------------|------------------|-------------|------------------|
| Balance, January 1          | \$          | 4,552,714        | \$          | 3,300,937        |
| Foreign exchange            | \$          | (33,808)         | \$          | (37,187)         |
| Short term loans received   |             | 2,401,065        |             | 1,600,170        |
| Repayment of principals     |             | (1,604,000)      |             |                  |
| <b>Balance, June 30</b>     | <b>\$</b>   | <b>5,315,971</b> | <b>\$</b>   | <b>4,863,920</b> |
| Foreign exchange            |             |                  | \$          | 404,240          |
| Short term loans received   |             |                  |             |                  |
| Repayment of principals     |             |                  |             | (715,446)        |
| <b>Balance, December 31</b> | <b>\$</b>   | <b>5,315,971</b> | <b>\$</b>   | <b>4,552,714</b> |

  

| <b>Outstanding balance at:</b>                   | <b>2012</b> |                  | <b>2011</b> |                  |
|--|-------------|------------------|-------------|------------------|
| a) Short term loan received on May 27, 2009      | \$          | 2,107,971        | \$          | 1,320,714        |
| b) Short term loan received on February 18, 2011 |             | -                |             | 1,616,000        |
| c) Short term loan received on November 17, 2011 |             | 1,604,000        |             | 1,616,000        |
| d) Short term loan received on March 14, 2012    |             | 1,604,000        |             | -                |
|  | <b>\$</b>   | <b>5,315,971</b> | <b>\$</b>   | <b>4,552,714</b> |

As at June 30, 2012, the Company had total short term loans outstanding of RMB33,141,964 (equivalent to \$5,315,971). As of December 31, 2011, the Company had total short term loans of RMB 28,172,735 (equivalent to \$4,552,714). The outstanding short term loans were comprised of the following facilities:

a) On May 27, 2009, RMB 5,000,000 (equivalent to \$770,000 as of December 31, 2009) was received from Standard Chartered Bank. The loan bears variable interest at prime plus 1.25% per annum. This loan is revolving every six months. During the year ended December 31, 2010, the Company made a repayment of RMB1,000,000 (equivalent to \$152,219) in June 2010. On June 22, 2010, the agreement has been renewed to June 21, 2015 and extended the loan limit to RMB10,000,000 (equivalent to \$1,539,000 as of December 31, 2010) with 90 day revolving credit and it bears variable interest rate at prime plus 1.25% per annum. On October 20, 2011, there is an additional agreement to extend the loan limit to RMB14,000,000 (equivalent to \$2,245,600 as of June 30, 2012) with 90 day revolving credit and bears variable interest rate at prime plus 2.75% per annum with the same expiry date. The outstanding loan balance is RMB 13,141,966 (equivalent to \$2,107,971) as of June 30, 2012 (December 31, 2011 – RMB 8,172,735 equivalent to \$1,320,714).

b) On February 18, 2011, RMB10,000,000 (equivalent to \$1,616,000 as of December 31, 2011) was received from China Construction Bank. The loan has a term of one year and bears fixed interest at 6.06% per annum. Monthly interest payment applies and the principal amount is due on February 17, 2012. As of June 30, 2012, the loan balance has been fully repaid.

c) On November 17, 2011, RMB10,000,000 (equivalent to \$1,616,000 as of December 31, 2011) was received from the Bank of Communications. The loan has a term of one year and bears fixed interest at prime rate times 1.3 per annum. Quarterly interest payment applies and the principal amount of RMB1M is due on November 1, 2012 and the remaining principal amount of RMB9M is due on November 16, 2012. As of June 30, 2012, the outstanding loan balance is RMB10,000,000 (equivalent to \$1,604,000 as of June 30, 2012).

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d) On March 14, 2012, RMB10,000,000 (equivalent to \$1,586,000 as of March 31, 2012) was received from the China Construction Bank. The loan has a term of one year and bears fixed interest at prime rate times 1.35 per annum. Monthly interest payment applies and the principal amount of RMB10M is due on March 13, 2013. As of June 30, 2012, the outstanding loan balance is RMB10,000,000 (equivalent to \$1,604,000 as of June 30, 2012).

The prime rate for short term loans in China was 5.31% in 2009. In 2010, the People's Bank of China announced an increase of 0.25% in its benchmark interest rate twice, on October 20, 2010 and December 26, 2010, which resulted in a prime rate of 5.81%. In 2011, the benchmark interest rate has been raised three times, each time at 0.25%, on February 8, 2011, April 6, 2011 and July 6, 2011. On June 8, 2012, the benchmark interest rate for one year loan has been reduced by 0.25%. As of June 30, 2012, the benchmark interest rate is at 6.31%.

During the three month and six month period ended Jun 30, 2012, the Company recorded total interest expense of \$113,421 and \$197,995 (2011 - \$88,404 and \$149,214 offset by \$22,350 (RMB150,000), a government subsidy for business on interest expense was received in May, 2011 for interest expensed in 2010.).

**Note 12 - Long Term Loan**

As at June 30, 2012, the Company has no long-term loan outstanding.

A Long Term loan of RMB 800,000 received from Standard Chartered Bank in China on April 27, 2009 bearing an interest at 21% and repayable in 36 monthly installments at approximately \$4,600 per month starting from May 27, 2009 to April 27, 2012. The carrying value of the loan is RMBnil (equivalent to \$nil) as of June 30, 2012 (December 31, 2011 – RMB115,465 equivalent to \$18,659). Within this amount, RMBnil (equivalent to \$nil) is due within one year and classified as a current liability as of June 30, 2012 (December 31, 2011 – RMB115,465 equivalent to \$18,659).

During the three month and six month period ended June 30, 2012, \$82 and \$809 (same period in 2011 - \$4,637 and \$9,786) of interest paid on the long-term loan was recognized in expenses.

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**Note 13 - Share Capital**

The authorized share capital of the Company is an unlimited number of common shares without par value.

|  | Number of<br>Shares | Share<br>Capital | Reserves     |            |
|--|---------------------|------------------|--------------|------------|
|  |                     |                  | Warrants     | Options    |
| <b>Balance, December 31, 2009</b>                    | 31,361,285          | \$ 5,610,417     | \$ 2,606,979 | \$ 724,419 |
| Fair value of options granted on November 10, 2009   |                     |                  |              | 7,055      |
| Shares issued by private placement on June 17, 2010  | 7,000,000           | 350,000          |              |            |
| -Issuance cost                                       |                     | (5,152)          |              |            |
| <b>Balance, December 31, 2010</b>                    | 38,361,285          | \$ 5,955,265     | \$ 2,606,979 | \$ 731,474 |
| Shares issued by private placement on April 28, 2011 | 6,100,000           | 650,953          | 145,102      |            |
| -Issuance cost                                       |                     | (22,871)         |              |            |
| Fair value of options granted on August 29, 2011     |                     |                  |              | 34,229     |
| Fair value of options granted on December 7, 2011    |                     |                  |              | 68,906     |
| Options exercised                                    | 180,000             | 23,200           |              | (7,200)    |
| Options expired                                      |                     | 88,460           |              | (88,460)   |
| <b>Balance, December 31, 2011</b>                    | 44,641,285          | \$ 6,695,007     | \$ 2,752,081 | \$ 738,948 |
| Fair value of options granted on August 29, 2011     |                     |                  |              | 6,340      |
| Fair value of options granted on December 7, 2011    |                     |                  |              | 16,037     |
| Warrants exercised                                   | 50,000              | 11,830           | (2,328)      |            |
| Option expired                                       |                     | 1,530            |              | (1,530)    |
| <b>Balance, March 31, 2012</b>                       | 44,691,285          | \$ 6,708,367     | \$ 2,749,753 | \$ 759,795 |
| Fair value of options granted on August 29, 2011     |                     |                  |              | 6,340      |
| Fair value of options granted on December 7, 2011    |                     |                  |              | 16,037     |
| Warrants exercised                                   | 850,000             | 201,087          | (39,587)     |            |
| Warrants expired                                     |                     | 100,132          | (100,132)    |            |
| Option exercised                                     | 30,000              | 2,700            |              | (1,200)    |
| Share Issuance cost (warrants expired)               |                     | 3,055            | (3,055)      |            |
| <b>Balance, June 30, 2012</b>                        | 45,571,285          | \$ 7,015,340     | \$ 2,606,979 | \$ 780,972 |

On June 17, 2010, the Company completed a private placement for 7,000,000 common shares at a price of \$0.05 per share for total gross proceeds of \$350,000. All shares issued with respect to the private placement are subject to a hold period that expires four months and a day from the closing. In connection with the private placement, the Company paid legal fees of \$5,152 as share issuance costs.

On April 28, 2011, the Company completed another private placement for 6,100,000 common shares at a price of \$0.13 per share for total gross proceeds of \$793,000. Each Unit consisted of one common share (a "Share") and one-half of a share purchase warrant (a "Warrant"). Each whole Warrant entitles the holder to purchase one Share at a price of \$0.19 for a period of one year from the date of issue. All shares issued with respect to the private placement are subject to a hold period that expires four months and a day from the closing. In connection with the private placement, the Company paid legal fees of \$7,041 and a cash commission \$12,740, equal to 7% of the gross proceeds derived from the sale of units placed by each of Mackie Research Capital Corporation ("Mackie") and Raymond James Ltd. In addition, the Company issued to Mackie the number of compensation warrants representing 5% of the number of units placed by Mackie. These are all under share issuance costs.

**Stock option plan**

The Company has established three stock option plans under which stock options to purchase common shares may be granted to directors, officers and employees of the Company and to any other person or Company permitted by the applicable regulatory authorities to purchase unissued

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common shares. The aggregate number of Shares issuable upon the exercise of all options granted under the plan shall not exceed 10% of the common shares of the corporation.

|                                | 2012              |                                      | 2011              |                                      |
|--------------------------------|-------------------|--------------------------------------|-------------------|--------------------------------------|
|                                | Number of options | Weighted average exercise price (\$) | Number of options | Weighted average exercise price (\$) |
| Outstanding, beginning of year | 2,279,000         | 0.26                                 | 1,590,000         | 0.26                                 |
| Exercised                      | (30,000)          | 0.05                                 | (180,000)         | 0.09                                 |
| Expired                        | (9,000)           | 0.30                                 | (481,000)         | 0.28                                 |
| Outstanding, June 30           | 2,240,000         | 0.19                                 | 929,000           | 0.28                                 |
| Exercisable, June 30           | 1,540,000         | 0.21                                 | 929,000           | 0.28                                 |

On January 2, 2009, the Company granted 200,000 new options at an exercise price of \$0.12 to one of its officers. These granted options vested 50% immediately and 50% to be vested in one year. The options are exercisable over 5 years. The grant date fair value of options was \$0.04.

On November 10, 2009, the Company granted 410,000 new options at an exercise price of \$0.05 to its employees, officers and directors. Granted options vested 50% immediately and 50% to be vested in one year. The options are exercisable over 5 years. The grant date fair value of options was \$0.04.

On August 29, 2011, the Company granted 400,000 new options at an exercise price of \$0.15 to its employees, officers and directors. Granted options vested 50% immediately and 50% to be vested in one year. The options are exercisable over 5 years. The grant date fair value of options was \$0.13.

On December 7, 2011, the Company granted 1,000,000 new options at an exercise price of \$0.15 to its employees, officers and directors. Granted options vested 50% immediately and 50% to be vested in one year. The options are exercisable over 5 years. The grant date fair value of options was \$0.13.

Amount expired is due to fully vested option expired. Amount forfeited is due to the cancellation of consulting services with consultants, the termination of employment during the vesting period or in the case options vested, options were out of the money.

There were 30,000 options being exercised at exercise price of \$0.05 and 9,000 options being expired at exercise price of \$0.30 during the six month period ended June 30, 2012.

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| Exercise Price (\$) | Options Outstanding |   | Options Exercisable |   |
|---------------------|---------------------|---|---------------------|---|
|                     | Number of options   | Weighted average remaining life (Years) | Number of options   | Weighted average remaining life (Years) |
| 0.05                | 150,000             | 2.36                                    | 150,000             | 2.36                                    |
| 0.15                | 1,400,000           | 4.36                                    | 700,000             | 4.36                                    |
| 0.30                | 690,000             | 0.89                                    | 690,000             | 0.89                                    |
|                     | 2,240,000           | 3.16                                    | 1,540,000           | 2.61                                    |

### **Assumptions**

The fair value of the options and warrants has been estimated by using the Black-Scholes option pricing model with the following assumptions:

|                         |                   |
|-------------------------|-------------------|
| Risk-free interest rate | 1.30 - 3.85%      |
| Dividend yield          | -                 |
| Volatility              | 80% - 150%        |
| Expected life           | 1 year to 5 years |

### **Warrants**

|                                | 2012               |                                      | 2011               |                                      |
|--------------------------------|--------------------|--------------------------------------|--------------------|--------------------------------------|
|                                | Number of warrants | Weighted average exercise price (\$) | Number of warrants | Weighted average exercise price (\$) |
| Outstanding, beginning of year | 3,100,000          | 0.19                                 | -                  | -                                    |
| Issued                         |                    |                                      | 3,100,000          | 0.19                                 |
| Exercised                      | (900,000)          | 0.19                                 | -                  | -                                    |
| Expired                        | (2,200,000)        | 0.19                                 | -                  | -                                    |
| Outstanding, June 30           | -                  | -                                    | 3,100,000          | 0.19                                 |
| Exercisable, June 30           | -                  | -                                    | 3,100,000          | 0.19                                 |

Pursuant to the term of the private placement took place on April 28, 2011, the Company issued 3,100,000 share purchase warrants with an exercise price of \$0.19 exercisable for a period of one year from the date of issue. Within the warrants issued, 50,000 warrants were issued to Mackie Research as part of the finder's fee.

During the 6 month period ended June 30, 2012, 900,000 warrants were being exercised at \$0.19 and 2,200,000 expired as on April 28, 2012.

### **Note 14 - Related Party Transactions**

The Company had the following transactions with directors and officers of the Company:



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|                              | Three months ended |               | Six months ended |               |
|------------------------------|--------------------|---------------|------------------|---------------|
|                              | June 30, 2012      | June 30, 2011 | June 30, 2012    | June 30, 2011 |
| Short-term employee benefits |                    |               |                  |               |
| - Salaries and severance     | \$ 42,900          | \$ 39,300     | \$ 85,800        | \$ 89,315     |
| - Professional fees          | 18,000             | 15,750        | 36,000           | 31,500        |
| - Director fees              | 4,000              | 2,200         | 8,000            | 4,400         |
|                              | \$ 64,900          | \$ 57,250     | \$ 129,800       | \$ 125,215    |
| Share-based payments         | 4,132              | -             | 8,219            | -             |
|                              | \$ 69,032          | \$ 57,250     | \$ 138,019       | \$ 125,215    |

Short-term employee benefits correspond to the amounts paid during the year and share-based payments correspond to the amounts recorded as expenses. During the six month period ended June 30, 2012, the Company paid \$85,800 (same period in 2011: \$89,315) in salaries to its management. Also, the Company paid \$36,000 (same period in 2011: \$31,500) in professional fees to one of its officers and paid \$8,000 (same period in 2011: \$4,400) as director fees.

|  | June 30, 2012 | December 31, 2011 | June 30, 2011 |
|--|---------------|-------------------|---------------|
| Accounts payable                                   | \$ 67,419     | \$ 24,205         | \$ 12,240     |
| Due to Shareholders of Fireswirl Technologies Inc. | 471,336       | 282,954           | 106,593       |
| Due to Shareholders of XCXD                        | 125,988       | 714,591           | 399,856       |
|  | \$ 664,743    | \$ 1,021,750      | \$ 518,689    |

As of June 30, 2012, the accounts payable balance included \$67,419 (December 31, 2011: \$24,205) incurred from regular operational expenses outstanding to officers of the company. As of June 30, 2012, the Company also had \$471,336 (December 31, 2011: \$282,954) due to a shareholder of Fireswirl Technologies Inc. (December 31, 2011: \$282,954) and \$125,988 due to a shareholder of XCXD (December 31, 2011: \$714,591).

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.

**Note 15 - Segmented Information**

The Company's sales revenues are allocated to geographic segments as follows:

|                | Three Months Ended |               | Six Months Ended |               |
|----------------|--------------------|---------------|------------------|---------------|
|                | June 30, 2012      | June 30, 2011 | June 30, 2012    | June 30, 2011 |
| China          | \$ 5,811,725       | \$ 4,959,104  | \$ 9,273,102     | \$ 9,128,532  |
| United Kingdom | 5,579              | 7,887         | 17,372           | 7,887         |
| USA            | 12,874             | 34,984        | 27,545           | 42,528        |
|                | \$ 5,830,178       | \$ 5,001,975  | \$ 9,318,019     | \$ 9,178,946  |

No customer accounted for greater than 10% of the Company's sale during the six month period ended June 30, 2012 and 2011.

The Company's long-term assets are located in Canada and China at June 30, 2012 as follows:

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|                | <b>China</b>      | <b>Canada</b>   | <b>Total</b>      |
|----------------|-------------------|-----------------|-------------------|
| Capital Assets | \$ 254,410        | \$ 4,938        | \$ 259,348        |
| Goodwill       | 306,926           |                 | 306,926           |
| Trademark      | 19,176            |                 | 19,176            |
| <b>Total</b>   | <b>\$ 580,512</b> | <b>\$ 4,938</b> | <b>\$ 585,450</b> |

The Company's long-term assets are located in Canada and China at December 31, 2011 as follows:

|                | <b>China</b>      | <b>Canada</b>   | <b>Total</b>      |
|----------------|-------------------|-----------------|-------------------|
| Capital Assets | \$ 303,832        | \$ 4,479        | \$ 308,311        |
| Goodwill       | 306,926           |                 | 306,926           |
| Trademark      | 19,176            |                 | 19,176            |
| <b>Total</b>   | <b>\$ 629,934</b> | <b>\$ 4,479</b> | <b>\$ 634,413</b> |

### **Note 16 - Credit Risk and Financial Instruments**

#### **Credit risk**

The Company grants credit to its customers in the normal course of business. Credit evaluations are performed on a regular basis and the financial statements take into account an allowance for bad debts. The business also depends on new customers using the product and there is additional risk when credit is granted to new and unproven customers. Credit evaluations are also performed on new customers.

There were no overdue accounts receivables outstanding as of June 30, 2012. As at June 30, 2012, there is one individual balance over 10% of the total AR Balance and accounted for \$1,165,368 (RMB7,265,387) while as at December 31, 2011, \$717,688 (RMB4,441,140) due from one customer balance over 10% of the total AR Balance was included in the balance of accounts receivable.

#### **Currency risk**

Foreign currency exchange rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Company uses the Canadian dollar as its reporting currency for these consolidated financial statements. The Company operates internationally, giving rise to exposure to market risks from changes in foreign exchange rates. The Company currently does not use derivative instruments to hedge its exposure to those risks. Most of the Company's businesses are organized geographically so that many of its expenses are incurred in the same currency as its revenues thus mitigating some of its exposure to currency fluctuations.

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|                             | June 30, 2012              | December 31, 2011          | June 30, 2011             |
|-----------------------------|----------------------------|----------------------------|---------------------------|
| US dollars:                 |                            |                            |                           |
| - Cash and cash equivalents | \$1,827 (US\$1,793)        | \$339 (US\$333)            | \$4,022(US\$4,151)        |
| - Accounts receivable       | \$6,950 (US\$6,820)        | \$16,517 (US\$16,269)      | \$36,639(US\$37,997)      |
| Hong Kong Dollars           |                            |                            |                           |
| - Cash and cash equivalents | \$3,307 (HK\$25,170)       | \$1,736 (HK\$13,266)       | \$26,097(HK\$210,557)     |
| - Accounts receivable       |                            | \$2,618 (HK\$20,000)       |                           |
| China Yuan Renminbi         |                            |                            |                           |
| - Cash and cash equivalents | \$196,973 (¥ 1,228,014)    | \$68,441 (¥ 423,521)       | \$354,704(¥ 2,377,436)    |
| - Restricted cash           | \$1,924,800 (¥ 12,000,000) | \$1,696,800 (¥ 10,500,000) | \$1,850,080(¥ 12,400,000) |
| United Kingdom Pounds       |                            |                            |                           |
| - Accounts receivable       | \$33,271 (£20,815)         | \$3,950 (£2,500)           | \$3,960(£2,500)           |

**Foreign currency sensitivity analysis**

The Company is mainly exposed to fluctuations in the Chinese RMB, US dollar and HK dollar. The major currency exposures, as of June 30, 2012, are summarized in Canadian dollar equivalents in the following table. The local currency amounts have been converted to Canadian dollar equivalents using the year end exchange rates.

|                                     | Chinese RMB in CAD | US dollar in CAD | HK dollar in CAD |
|-------------------------------------|--------------------|------------------|------------------|
| Cash                                | \$ 196,973         | \$ 1,827         | \$ 3,307         |
| Restricted cash                     | 1,924,800          | -                | -                |
| Accounts Receivable                 | 1,428,800          | 6,950            | -                |
| Other financial assets              | 938,544            | -                | 56,357           |
| Accounts payable and accrued liabil | (1,004,768)        | -                | (140,705)        |
| Other financial liabilities         | (5,315,971)        | -                | -                |
| Shareholder loans                   | (125,988)          | -                | (471,336)        |
| Net financial assets                | \$ (1,957,610)     | \$ 8,777         | \$ (552,377)     |

The following table details the Company's sensitivity, with regards to the above net asset position, to a 1% strengthening of the Chinese RMB, US dollar and HK dollar, against the Canadian dollar. The sensitivity analysis includes foreign currency denominated monetary assets and liabilities and adjusts their translation at period end for a 1% change in foreign currency rates. For a 1% weakening against the Canadian dollar, there would be an equal and opposite impact on net income and comprehensive income.

|                      | Chinese RMB in CAD | US dollar in CAD | HK dollar in CAD |
|----------------------|--------------------|------------------|------------------|
| Net income           | \$ (19,576)        | \$ 88            | \$ (5,524)       |
| Comprehensive income | \$ (19,576)        | \$ 88            | \$ (5,524)       |

**Fair Value**

Fair value is the amount at which a financial instrument could be exchanged between willing parties based on current markets for instruments with the same risk, principal and remaining maturity. Fair value estimates are based on present value and other valuation techniques using rates that reflect those that the Company could currently obtain, on the market, for financial instruments with similar terms, conditions and maturities.

The fair value hierarchy established by CICA Handbook Section 3862 – Financial Instruments – Disclosures (“Section 3862”) establishes three levels to classify the inputs to valuation techniques used to measure fair value. The three levels of the fair value hierarchy are described below:

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Level 1 – Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 – Inputs that are observable, either directly or indirectly, but do not qualify as Level 1 inputs (i.e., quoted prices for similar assets or liabilities).

Level 3 – Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

The Company's financial instruments include cash, accounts receivable, HST recoverable, deposits and prepayments, accounts payable and accrued liabilities, short term loans, loans from shareholders, and long-term loans.

The fair value of accounts receivable, deposits and prepayments, loan receivable, accounts payable and accrued liabilities, and short term loans is approximately equal to their carrying values due to their short-term maturity.

The fair value of long-term loan approximates its amortized costs using the effective interest method.

The fair value of loan from shareholders could not be determined as there are no fixed terms of repayment.

The following table is a classification of fair value measurements recognized using a fair value hierarchy that reflects the significance of the inputs used in making the measurements as at June 30, 2012:

| Assets                    | Level 1      | Level 2 | Level 3 | Total        |
|---------------------------|--------------|---------|---------|--------------|
| Cash and Cash Equivalents | \$ 227,600   | \$ -    | \$ -    | \$ 227,600   |
| Restricted Cash           | 1,924,800    | -       | -       | 1,924,800    |
| Total Financial Assets    | \$ 2,152,400 | \$ -    | \$ -    | \$ 2,152,400 |

**Interest Risk**

The Company is exposed to interest rate risk on the utilized portion of its credit facilities and does not currently hold any financial instruments that mitigate this risk. Interest rate fluctuations on the current level of borrowings will have significant impact on company's financial position.

**Interest risk sensitivity analysis**

Management has completed a sensitivity analysis to estimate the impact on net loss for the period which a change in interest rates during the six month period ended June 30, 2012 would have had.

This sensitivity analysis includes the following assumption:

- Changes in foreign exchange rate do not cause a change in interest rates.

The impact on net loss of a +/- 5% change in the interest rate is +/- \$11,792 (same period 2011 - +/- \$6,854).

The above results arise primarily as a result of the Company bearing variable interest rates based on the prime rate for the short term loans and long term loan.

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**Limitations of sensitivity analysis**

The analysis above demonstrates the effect of a change in interest rates in isolation. There is a correlation between a change in interest rates and foreign exchange rate, which if considered could cause the results above to vary.

Additionally, the Company's financial position may vary at the time that a change in either of interest risk or foreign exchange rate occurs, causing the impact on the Company's results to differ from that shown above.

**Liquidity Risk**

The purpose of liquidity risk management is to maintain a sufficient amount of cash and cash equivalents. Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at excessive cost. The Company's growth is financed through a combination of the cash flows from operations and the issuance of equity. One of management's primary goals is to maintain an optimal level of liquidity through the active management of the assets and liabilities as well as the cash flows.

As at June 30, 2012, the Company has accounts payable and accrued liabilities of \$1,249,403 due within 12 months (December 31, 2011 - \$937,731). As at June 30, 2012 the Company has short term loans of \$5,315,971 (December 31, 2011 - \$4,552,714), see note 11. As at June 30, 2012, the Company is holding cash and cash equivalents of \$227,600 (December 31, 2011 - \$75,677).

The Company reported a net loss attributable to common shares of \$446,037 for the six month period ended June 30, 2012 compared to a net loss attributable to common shares of \$610,647 for the same period of 2011, representing a decrease in loss of 27%.

The continuation of the Company as a going concern is dependent upon its ability to raise additional financing and ultimately attain and maintain profitable operations. 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 consolidated 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.

In the event that cash flow from operations, if any, together with the proceeds of any future financings, are insufficient to meet the Company's current operating expenses, the Company will be required to re-evaluate its planned expenditures and allocate its total resources in such a manner as the Board of Directors and management deems to be in the Company's best interest. Given the Company's available liquid resources as compared to the timing of the payments of liabilities, access to financing, and improving financial performance, management assesses the Company's overall liquidity risk to be low.

**Note 17 - Commitments and Contingencies**

- (a) The Company has lease obligations to April 30, 2015. The future annual minimum payments under operating leases is \$20,406 to the end of this year and \$41,528 annually onward.
- (b) A foreign subsidiary Fireswirl Technologies (Shenzhen) Company Ltd. has a lease obligation of \$1,759 (RMB10,969) per month until the lease expires on September 12, 2012.

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(c) A foreign subsidiary XCXD has a lease obligation of \$10,934 (RMB68,166) per month until the lease expires on December 1, 2013.

(d) A foreign subsidiary XCXD has a lease obligation of \$74,600 in July 2011 as prepaid rent for a lease that will expire on September 14, 2012.

**Note 18- Capital Management**

The Company has defined its capital as capital stock, contributed surplus and retained earnings.

The following table summarizes certain information with respect to the Company's capital structure at the end of each period:

|                    |    | June 30, 2012 | December 31, 2011 |           | June 30, 2011 |           |
|--------------------|----|---------------|-------------------|-----------|---------------|-----------|
| Shareholder Equity | \$ | 921,485       | \$                | 1,248,785 | \$            | 1,449,269 |

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern, to maintain appropriate cash reserves on hand to support continued operations and shareholder returns, maintain capital structure while keeping capital costs at a minimum, and to invest cash on hand in highly liquid, highly rated financial instruments.

The company is not exposed to externally imposed capital restrictions, and the Company's objectives and strategies described above have not changed since last year. These objectives and strategies are reviewed on a continuous basis.

The Company normally finances its property and equipment purchases with cash.

**Note 19 – Supplemental Disclosure with Respect to Cash Flows**

|   | Three months ended |               | Six months ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 30, 2012      | June 30, 2011 | June 30, 2012    | June 30, 2011 |
| Cash paid during the period for interest    | \$113,582          | \$90,932      | \$198,804        | \$154,925     |
| Cash paid during the eriod for income taxes | \$0                | \$0           | \$0              | \$4,551       |

During the six month period ended June 30, 2012, cash used in Income taxes of \$nil were incurred from XCXD's operations in China (same period in 2011 - \$4,551).

There were no significant non-cash transactions during the six month period ended June 30, 2012 and 2011.

**Note 20 - Subsequent Event**

There is no subsequent event.

**Note 21 – Comparative Figures**

Certain comparative figures have been reclassified to conform to the current year's presentation.