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REPORT OF INDEPENDENT REGISTERED CHARTERED ACCOUNTANTS

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF POINTS INTERNATIONAL LTD.

We have audited the internal control over financial reporting of Points International Ltd. and subsidiaries (the "Company") as of December 31, 2007, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

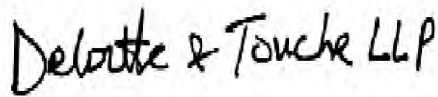
Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement or the company's annual or interim statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in management's assessment: As a result of the restatements reflected in the December 31, 2007 financial statements and audit adjustments related thereto, the Company has concluded that there is a material weakness in internal control over financial reporting as of December 31, 2007. The Company has not demonstrated the timely and in-depth involvement of external resources to supplement their knowledge of generally accepted accounting principles, particularly with respect to complex revenue recognition matters related to upfront contract initiation fees in prior years. Given that the current internal controls did not detect these past errors, a material weakness existed as of December 31, 2007. This material weakness was

considered in determining the nature, timing and extent of audit tests applied in our audit of the consolidated financial statements as of and for the year ended December 31, 2007, of the Company and this report does not affect our report on such financial statements.

In our opinion, because of the effect of the material weakness identified above on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of December 31, 2007, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of the Company as of and for the year ended December 31, 2007 and our report dated March 19, 2008 expressed an unqualified opinion on those financial statements and included a separate report titled Comments by Independent Registered Chartered Accountants on Canada-United States of America Reporting Difference referring to changes in accounting principles.

The image shows a handwritten signature in black ink that reads "Deloitte & Touche LLP". The signature is written in a cursive, professional style.

Independent Registered Chartered Accountants
Licensed Public Accountants
Toronto, Canada
March 19, 2008

Deloitte.

Report of Independent Registered Chartered Accountants

To the Board of Directors and Shareholders of Points International Ltd.

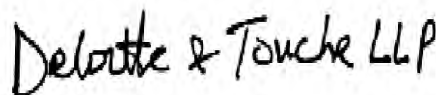
We have audited the accompanying consolidated balance sheet of Points International Ltd. and subsidiaries (the “Company”) as at December 31, 2007, and the related consolidated statements of operations, comprehensive loss and deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2007, based on the criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 19, 2008 expressed an adverse opinion on the Company’s internal control over financial reporting because of a material weakness.

The consolidated financial statements as of December 31, 2006 and for the year then ended (as restated) were audited by Mintz & Partners LLP who expressed an opinion without reservation on those statements in their report dated March 7, 2007 except for Note 4, which is as of March 19, 2008.



Independent Registered Chartered Accountants
Licensed Public Accountants
Toronto, Canada
March 19, 2008



**Comments by Independent Registered Chartered Accountants on
Canada-United States of America Reporting Difference**

The standards of the Public Company Accounting Oversight Board (United States) require the addition of an explanatory paragraph (following the opinion paragraph) when there are changes in accounting principles that have a material effect on the comparability of the Company's financial statements, such as the changes described in Note 2(p) to the consolidated financial statements. Our report to the Board of Directors and Shareholders, dated March 19, 2008, is expressed in accordance with Canadian reporting standards which do not require a reference to such changes in accounting principles in the auditors' report when the changes are properly accounted for and adequately disclosed in the financial statements.

Deloitte & Touche LLP

Independent Registered Chartered Accountants
Licensed Public Accountants
Toronto, Canada
March 19, 2008



Auditors' Report

To the Shareholders of Points International Ltd.

We have audited the accompanying consolidated balance sheet of Points International Ltd. and subsidiaries (the "Company") as at December 31, 2006, and the related consolidated statements of operations, comprehensive loss and deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Points International Ltd. and subsidiaries as at December 31, 2006, and the results of their operations and their cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

As described in Note 4 to the consolidated financial statements, the accompanying consolidated financial statements of the Company as of December 31, 2006 and for the year then ended have been restated. We therefore amended our previous report dated March 7, 2007 on those financial statements based on our audit of the effect of the restatement to the Company's restated financial statements as of December 31, 2006 and for the year then ended.

Mintz & Partners LLP

Toronto, Ontario
March 7, 2007 except for Note 4,
which is as of March 19, 2008

Chartered Accountants
Licensed Public Accountants

CONSOLIDATED BALANCE SHEETS*(Expressed in Canadian Dollars)*

POINTS INTERNATIONAL LTD.

AS AT	December 31, 2007	Restated (Note 4) December 31, 2006
ASSETS		
CURRENT		
Cash and cash equivalents (Note 5)	\$ 21,148,331	\$ 19,758,490
Funds receivable from payment processors (Note 6)	5,034,223	3,710,341
Short-term investments (Note 7)	7,272,200	–
Security deposits (Note 8)	1,533,073	1,220,209
Accounts receivable (Note 9)	3,293,291	2,375,966
Current portion of future income tax asset (Note 22)	590,000	–
Current portion of deferred costs (Note 12)	274,327	283,649
Prepays and sundry assets	<u>1,735,538</u>	<u>2,059,212</u>
	<u>40,880,983</u>	<u>29,407,867</u>
PROPERTY AND EQUIPMENT (Note 10)	1,981,463	2,934,239
INTANGIBLE ASSETS (Note 11)	1,384,080	1,986,433
GOODWILL (Note 11)	4,129,069	4,129,069
DEFERRED COSTS (Note 12)	474,973	1,383,446
FUTURE INCOME TAX ASSET (Note 22)	<u>–</u>	<u>590,000</u>
	<u>7,969,585</u>	<u>11,023,187</u>
	<u>\$ 48,850,568</u>	<u>\$ 40,431,054</u>
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	\$ 3,425,150	\$ 3,342,869
Current portion of deferred revenue	1,600,194	776,251
Payable to loyalty program partners	30,195,664	21,000,403
Current portion of loan payable (Note 13)	<u>5,820</u>	<u>33,515</u>
	<u>35,226,828</u>	<u>25,153,038</u>
DEFERRED REVENUE	380,047	422,476
LOAN PAYABLE (Note 13)	–	5,289
CONVERTIBLE PREFERRED SHARES (Note 15)	<u>20,306,850</u>	<u>19,506,279</u>
	<u>55,913,725</u>	<u>45,087,082</u>
SHAREHOLDERS' DEFICIENCY		
CAPITAL STOCK (Note 16)	45,994,159	43,051,048
WARRANTS (Note 17)	30,668	186,688
CONTRIBUTED SURPLUS (Note 17(g))	7,945,633	8,703,518
DEFICIT	<u>(61,033,617)</u>	<u>(56,597,282)</u>
	<u>(7,063,157)</u>	<u>(4,656,028)</u>
	<u>\$ 48,850,568</u>	<u>\$ 40,431,054</u>

APPROVED ON BEHALF OF THE BOARD:Doug Carty
DirectorRob Maclean
Director

CONSOLIDATED STATEMENT OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT*(Expressed in Canadian Dollars)*

POINTS INTERNATIONAL LTD

FOR THE YEARS ENDED DECEMBER 31	2007	Restated (Note 4) 2006
REVENUE		
Principal	\$ 20,109,876	\$ 3,099,182
Commission	10,780,678	8,373,966
Interest	<u>717,146</u>	<u>222,555</u>
	<u>31,607,700</u>	<u>11,695,703</u>
GENERAL AND ADMINISTRATION EXPENSES		
Direct cost of principal revenue	14,585,813	–
Employment costs	9,291,645	8,157,264
Sales commissions and related expenses	1,618,877	818,187
Marketing and communications	1,650,075	2,607,609
Technology services	918,140	1,055,967
Amortization of property and equipment	1,817,783	1,702,535
Amortization of intangible assets	760,495	890,346
Amortization of deferred costs	472,794	531,699
Foreign exchange loss	547,186	9,319
Operating expenses (Note 18)	<u>3,159,014</u>	<u>2,739,527</u>
	<u>34,821,822</u>	<u>18,512,453</u>
OPERATING LOSS – before undernoted	<u>(3,214,122)</u>	<u>(6,816,750)</u>
OTHER EXPENSES		
Interest on preferred shares	1,168,728	1,109,823
Interest and other charges	53,485	64,737
Interest on convertible debentures	<u>–</u>	<u>194,753</u>
	<u>1,222,213</u>	<u>1,369,313</u>
NET LOSS AND COMPREHENSIVE LOSS	\$ <u>(4,436,335)</u>	\$ <u>(8,186,063)</u>
LOSS PER SHARE (Note 19)	\$ <u>(0.04)</u>	\$ <u>(0.08)</u>
DEFICIT – Beginning of year		
As previously reported	\$ (55,335,455)	\$ (47,428,760)
Effect of restatement of prior years (Note 4)	<u>(1,261,827)</u>	<u>(982,459)</u>
As restated	(56,597,282)	(48,411,219)
NET LOSS	<u>(4,436,335)</u>	<u>(8,186,063)</u>
DEFICIT – End of year	\$ <u>(61,033,617)</u>	\$ <u>(56,597,282)</u>

CONSOLIDATED STATEMENTS OF CASH FLOWS*(Expressed in Canadian Dollars)*

FOR THE YEARS ENDED DECEMBER 31	2007	Restated (Note 4) 2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Loss	\$ (4,436,335)	\$ (8,186,063)
Items not affecting cash		
Amortization of property and equipment	1,817,783	1,702,535
Amortization of deferred costs	472,794	531,699
Amortization of intangible assets	760,495	890,346
Unrealized foreign exchange loss / (gain)	(481,094)	185,511
Employee stock option expense (Note 17)	583,934	366,981
Interest on Series Two and Four Preferred Shares	1,168,728	1,109,823
Interest accrued on convertible debentures	–	194,753
Changes in non-cash balances related to operations (Note 20(a))	<u>11,131,320</u>	<u>5,234,058</u>
CASH FLOWS PROVIDED BY OPERATING ACTIVITIES	<u>11,017,625</u>	<u>2,029,643</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to property and equipment	(865,008)	(1,029,936)
Additions to intangible assets	(158,142)	(115,164)
Purchase of short-term investments	(7,272,200)	–
Sales of short-term investments	–	2,348,418
Payments for the acquisition of MilePoint, Inc.	–	(400,000)
CASH FLOWS PROVIDED BY (USED IN) INVESTING ACTIVITIES	<u>(8,295,350)</u>	<u>803,318</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of loan payable (Note 13)	(32,984)	(29,818)
Issuance of capital stock (Note 16)	1,445,272	437,887
CASH FLOWS PROVIDED BY FINANCING ACTIVITIES	<u>1,412,288</u>	<u>408,069</u>
EFFECT OF EXCHANGE RATE CHANGES ON CASH HELD IN FOREIGN CURRENCY	<u>(2,744,722)</u>	<u>287,590</u>
INCREASE IN CASH AND CASH EQUIVALENTS	<u>1,389,841</u>	<u>3,528,620</u>
CASH AND CASH EQUIVALENTS – Beginning of the year	<u>19,758,490</u>	<u>16,229,870</u>
CASH AND CASH EQUIVALENTS – End of the year	<u>\$ 21,148,331</u>	<u>\$ 19,758,490</u>

1. BASIS OF PRESENTATION AND BUSINESS OF THE CORPORATION

The accompanying consolidated financial statements of Points International Ltd. (the "Corporation") include the financial position, results of operations and cash flows of the Corporation and its wholly owned subsidiaries, Points.com Holdings Inc., Points International (US) Ltd. and Points International (UK) Limited and its indirect wholly owned subsidiary, Points.com Inc.

The Corporation operates in one segment, providing web-based solutions to the loyalty program industry. The range of *Ecommerce Services* include the retailing and wholesaling of loyalty program currencies, a range of additional ecommerce products that enhance either the loyalty program's consumer offering or its backend operations, and management of an online consumer-focused loyalty points management web-portal.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). Note 28 describes and reconciles the significant measurement differences between Canadian and United States generally accepted accounting principles ("US GAAP") affecting the accompanying consolidated financial statements. A summary of significant accounting policies is set out below:

a) Use of estimates

The preparation of these consolidated financial statements has required management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities as at December 31, 2007 and 2006 and the revenues and expenses reported for the years then ended. On an ongoing basis, the Corporation evaluates its estimates, including those related to provisions for doubtful accounts, the provision for transaction losses (credit card chargebacks), income taxes, stock-based compensation, revenue recognition, goodwill and intangible assets. The Corporation bases its estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from those estimates.

b) Revenue recognition

The Corporation's revenue is categorized as principal, commission, and interest and is generated through the technology services provided to loyalty program partners. Revenue is recognized when evidence of an arrangement exists, the fee is fixed and determinable, services have been provided, and collection of the receivable is reasonably assured.

The Corporation's revenue has been categorized as follows:

Principal Revenue

Principal revenue groups together several streams of revenue that the Corporation realizes in delivering services to the loyalty program industry. The following is a list of revenue streams and the related revenue recognition policy.

- (i) Technical design and development work is performed at the commencement of a business relationship with a loyalty program partner. The majority of the technical design and development fees are the up-front charges to cover the Corporation's cost of setting up the loyalty program web interface and customizing the look and feel of the site to that of the loyalty program partner. Once the loyalty program partner web site is functional, end consumers are able to transact on the site which gives rise to transactional revenue for the term of the contract. These fees are recorded in accordance with Abstract 142 of the Emerging Issues Committee ("EIC-142") of the CICA Handbook, "Revenue Arrangements with Multiple Deliverables". As such, this revenue is deferred, along with direct related costs to the extent there is deferred revenue, and recognized over the term of the

contract, which approximates the period of expected benefit.

- (ii) Customized technical design service fees are also charged to loyalty program partners who require custom programming or web-design work that is not tied to an ongoing stream of revenue. This revenue is distinct from any other existing agreement and the delivered product has stand-alone value to the loyalty program partner. This revenue is recognized on a percentage of completion basis.
- (iii) Reseller revenue is a type of transactional revenue that is realized when the Corporation takes a principal role in the retailing and wholesaling of loyalty currency for loyalty program partners. The Corporation's role as a principal in the transaction is determined by the contractual arrangement in place with the loyalty program partner. In this instance, the Corporation has a substantive level of responsibility with respect to operations, marketing and commercial transaction support. As well, the Corporation assumes substantive credit and inventory risk with each transaction processed. Revenue earned as reseller revenue is recorded on a gross basis in accordance with Abstract 123 of the Emerging Issues Committee ("EIC-123") of the CICA Handbook, "Reporting Revenue Gross as a Principal versus Net as Agent". Related costs are recorded as part of direct costs of principal revenue.
- (iv) Loyalty program sign-up fees are charged to loyalty program partners at the commencement of a business relationship to gain access to the Corporation's proprietary *Points.com* web portal. This portal allows the end-consumers of loyalty programs to register and track the programs they participate in and allows them to transact loyalty currency in ways that are not possible within the core programs of the loyalty programs. The Corporation earns ongoing revenue from the ongoing transactions over the term of the contract. As such, in accordance with EIC-142 of the CICA Handbook, this revenue is deferred, along with direct related costs to the extent there is deferred revenue, and recognized over the term of the contract, which approximates the period of expected benefit.
- (v) Hosting fees are charged to certain loyalty program partners for the hosting of web-based services carried out by the Corporation. These fees are charged monthly to the loyalty program partners over the term of the contract. Revenue is recognized on a monthly basis over the term of the contract as it approximates the period of expected benefit.
- (vi) Management fees are charged to loyalty program partners who require custom marketing or non-technical solutions that are not covered by any other agreements with the Corporation. This revenue is recognized in the period that the service is provided.
- (vii) Membership support revenue relates to fees charged to end-consumers who have subscribed for an upgraded membership on the *points.com* web portal which gives them access to telephone support, exclusive contest access and additional bonus loyalty currency. Memberships are sold either on a monthly or annual basis. Revenue is recognized evenly over the term of the membership.

Commission Revenue

Commission revenue is a type of transactional revenue that is realized when the Corporation takes an agency role in the retailing and wholesaling of loyalty currency for loyalty program partners. The Corporation's role as an agent in the transaction is determined by the contractual arrangement in place with the loyalty program partner. In this instance, the Corporation has a minimal level of responsibility with respect to operations, marketing and commercial transaction support. As well, the Corporation assumes minimal credit and inventory risk with each transaction processed. Commission revenue is recorded on a net basis in accordance with EIC-123.

Interest Revenue

Interest revenue is earned on funds invested in accordance with the Corporation's Board approved Investment Policy. Interest revenue is recognized when earned on an accrual basis.

c) Cash and cash equivalents

Cash and cash equivalents include highly liquid investments, with original or remaining maturity dates of three months or less when purchased, and are carried at cost which approximates their fair value because of the short-term maturity of the instruments. These include cash and term deposits.

d) Funds receivable from payment processor

Funds receivable from payment processors are amounts collected on behalf of the Corporation by payment processors. The funds are held for up to three days before being released to the Corporation.

e) Short-term investments

Short-term investments consist of highly liquid investments (term deposits) with original maturity dates between three and twelve months, are classified as held to maturity, and are carried at amortized cost using the effective interest rate method. At the balance sheet date, amortized cost approximated market value.

f) Property and equipment

Property and equipment are recorded at cost less accumulated amortization. Amortization based on the estimated useful lives of the assets is provided using the methods and annual rates as follows:

Furniture and equipment	20% declining balance basis
Computer equipment	30% declining balance basis
Software	30% straight-line basis
Web site development and technology	straight-line over 3 years
Leasehold improvements	straight-line over 5 years

g) Intangible assets

Patents will be amortized over the useful life of the patent, commencing when the patents have been granted. As of December 31, 2007, the Corporation does not have any registered patents. Registered trademarks have been determined to have an indefinite life and are therefore not amortized.

The fair value of the contract-based intangible assets acquired as part of the Corporation's acquisition of the business assets of MilePoint, Inc. (see Note 11) are amortized over the useful lives of the related contracts.

For finite lived assets, the Corporation assesses impairment only if impairment indicators exist. If the carrying amount of the finite lived asset cannot be recovered from undiscounted cash flows, an appropriate amount will be charged to income as an "impairment charge" at that time.

The Corporation tests its' indefinite lived assets for impairment at least annually, to determine whether the carrying value exceeds the fair value. If it is determined that an impairment exists, such impairment it is recognized in net income at that time.

h) Goodwill

Goodwill represents the excess of the purchase price of acquired businesses over the estimated fair value of the tangible and intangible net assets acquired. Goodwill is not amortized. The Corporation tests goodwill for impairment at least annually, at each year end, and should an impairment be determined to exist, recognizes such impairment in net income at that time.

i) Deferred costs

Costs incurred in respect of certain financings are deferred and charged to income over the term of financing. Deferred finance charges represent legal and other related fees incurred to obtain the financing described in Note 15.

In relation to the Corporation's technology design and development revenue involving revenue arrangements with multiple deliverables, the Corporation incurs direct upfront contract initiation costs associated with the web site application design and development. Deferred costs related to the revenue streams are deferred to the extent of the deferred revenue. These costs are deferred over the expected life of the agreement.

Direct costs associated with securing key loyalty program partner relationships are amortized over the term of the relationship.

j) Payable to loyalty program partners

Payable to loyalty program partners include amounts collected through *Ecommerce Services* for retailing, wholesaling and other loyalty currency services. These amounts are payable to the loyalty program partners within 45 days.

k) Deferred revenue

Deferred revenue includes proceeds received in advance for technology design and development and membership fees for services to be provided over a future period. Deferred revenue also includes proceeds for mileage, where the issuance to loyalty program members will occur at a later date.

l) Translation of foreign currency

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at exchange rates prevailing at the balance sheet date for monetary items. Revenue and expenses are translated at average exchange rates prevailing during the year. Realized and unrealized foreign exchange gains and losses are accounted for and disclosed separately and are included in net earnings.

The results of foreign operations, which are financially and operationally integrated with the Corporation, are translated using the temporal method. Under this method, monetary assets and liabilities denominated in foreign currencies have been translated into the Corporation's functional currency, the Canadian dollar, at the rate of exchange prevailing at year end. Fixed assets have been translated at the rates prevailing at the dates of acquisition. Revenue and expense items are translated at the average rate of exchange for the year.

m) Income taxes

The Corporation uses the asset and liability method of accounting for income taxes. Future income tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carryforwards. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in tax rates is recognized in income in the year that includes the enactment or substantive enactment date.

The Corporation provides a valuation allowance for future tax assets when it is more likely than not that some portion or all of the future tax assets will not be realized.

n) Earnings per share

The Corporation uses Section 3500 ("Earnings per Share") of the CICA Handbook, which directs that the treasury stock and if-converted method be used to calculate diluted earnings per share.

Diluted earnings per share considers the dilutive impact of the exercise of outstanding stock options, warrants, and conversion of preferred shares, as if the events had occurred at the beginning of the period or at a time of issuance, if later.

o) Stock based compensation

Employees

The Corporation has a stock option plan for directors, officers and employees. Effective January 1, 2003, the Corporation adopted the amended recommendations of the CICA with respect to stock-based compensation and other stock-based compensation. The Corporation applies the fair value method to all grants of stock options. The fair value of options granted is estimated at the date of grant using the Black-Scholes option pricing model incorporating assumptions regarding risk-free interest rates, dividend yield, volatility factor of the expected market price of the Corporation's stock and a weighted average expected life of options. The estimated fair value of the options that are ultimately expected to vest based on performance-related conditions, as well as the options that are expected to vest based on future service, is recorded over the option's vesting period and charged to stock-based compensation. In determining the amount of options that are expected to vest, the Corporation takes into account voluntary termination behaviour as well as trends of actual option forfeitures. Any consideration paid on the exercise of stock options is credited to share capital.

Non employees

For stock based compensation issued to non employees, the Corporation recognizes an asset or expense based on the fair value of the equity instrument issued.

p) Changes in accounting policies

Effective January 1, 2007, the Corporation adopted the recommendations of the CICA Handbook Section 1530, Comprehensive Income; 3251, Equity; 3855, Financial Instruments – Recognition and Measurement; Section 3861, Financial Instruments – Measurement, Disclosure and Presentation; and Section 3865, Hedges. As required by the standards, the change in policies have been applied retrospectively with no restatement to prior periods.

Comprehensive income

Section 1530 establishes standards for reporting and display of comprehensive income. Unrealized gains or losses on available-for-sale investments, and the effective portion of gains or losses on derivatives designated as cash flow hedges and hedges of the net investment in self-sustaining foreign operations are included in other comprehensive income ("OCI" and accumulated other comprehensive income ("AOCI") is included as a separate component of equity. The Corporation had no such OCI or loss transactions for the year ended December 31, 2007 and there were no opening or closing balances for AOCI.

Financial instruments

Under the new standards, all financial instruments are classified into one of the following five categories: held-for-trading (assets and liabilities), available-for-sale financial assets, loans and receivables, held-to-maturity financial assets, and other financial liabilities. Transaction costs are included in the initial carrying amount of financial instruments except for held-for-trading items in which case

they are expensed as incurred. All financial instruments are initially measured at fair value. Measurement in subsequent periods depends on the classification of the financial instrument. Under the standards:

Held-for-trading (assets or liabilities)

This category is comprised of certain investments in equity and debt instruments, stand-alone derivatives, other than those designated as hedging items, and embedded derivatives requiring separation. They are carried in the balance sheet at fair value with changes in fair value recognized in the income statement.

Loans and receivables

These assets are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They arise principally through the provision of goods and services to customers (accounts receivable), but also incorporate other types of contractual monetary assets. They are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest rate method, less any provision for impairment.

Held-to-maturity investments

These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the company's management has the positive intention and ability to hold to maturity and comprises certain investments in debt securities. These assets are initially recognized at fair value and subsequently carried at amortized cost, using the effective interest rate method, less any provision for impairment.

Available-for-sale investments

Non-derivative financial assets not included in the above categories are classified as available-for-sale and comprises certain investments in equity instruments, including a company's investments in private companies. When they have a quoted market price in an active market, they are carried at fair value with changes in fair value recognized as a separate component of other comprehensive income. When they do not have a quoted market price in an active market, they are carried at cost. Where a decline in the fair value is determined to be other than temporary, the amount of the loss is removed from other comprehensive income and recognized in the income statement.

Other financial liabilities

Other financial liabilities includes all financial liabilities other than those classified as held-for-trading and comprises trade payables, other short-term monetary liabilities, and the debt element of convertible debt. These liabilities are initially recognized at fair value and subsequently carried at amortized cost using the effective interest rate method.

The adoption of these standards had no impact on the opening retained earnings and therefore did not result in a transitional adjustment as of January 1, 2007.

The Corporation's financial assets and liabilities are recorded and measured as follows:

Asset/Liability	Category	Measurement
Cash and cash equivalents	Held-for-trading	Fair value
Funds receivable from payment processors	Loans and receivables	Amortized cost
Short-term investments	Held-to-maturity	Amortized cost
Security deposits	Loans and receivables	Amortized cost
Accounts receivable	Loans and receivables	Amortized cost
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Deposits	Other liabilities	Amortized cost
Loan payable	Other liabilities	Amortized cost
Convertible preferred shares	Other liabilities	Amortized cost

Other balance sheet accounts, such as prepaid expenses, property and equipment, intangible assets, goodwill, future income tax asset, deferred costs, and deferred revenue are not within the scope of the new accounting standards as they are not financial instruments.

Hedges

The Corporation may use derivative instruments to manage foreign exchange and interest rate risk. The Corporation may choose to designate derivative instruments as hedges.

- **Cash flow hedges** – The effective portion of the changes in fair value of financial instruments designated as a cash flow hedge is recognized in OCI, net of tax, with any ineffective portion being recognized immediately in net income. Gains and losses are recovered from OCI and recognized in net income in the same period as the hedged item affects net income. If at any point the hedged transaction is no longer expected to occur, the cumulative gain or loss recognized in AOCI is reclassified to net income immediately
- **Fair value hedges** – Both the financial instrument designated as the hedging item, and the underlying hedged asset or liability are measured at fair value. Changes in the fair value of both the hedging and hedged item are reflected in net income immediately. The carrying value of the hedged item is adjusted through net income for changes in its fair value attributable to the hedged risk.

Net investment hedges – Foreign exchange gains and losses on debt designated as a net investment hedge are recognized in OCI, net of tax, to the extent the hedge is effective. The ineffective portion of such hedges is recognized in net income.

The Corporation had no such hedges for the years ended December 31, 2007 and December 31, 2006.

3. RECENT ACCOUNTING PRONOUNCEMENTS

Financial Instruments – Disclosure and Presentation

In December 2006, the CICA issued Section 3863, "Financial Instruments – Presentation", to enhance financial statement users' understanding of the significance of financial instruments to an entity's financial position, performance and cash flows. This Section establishes standards for presentation of financial instruments and non-financial derivatives. This Section replaces the existing requirement on the presentation of financial instruments which have been carried forward unchanged. It deals with the classification of financial instruments, from the perspective of the issuer, between liabilities and equity, the classification of related interest, dividends, losses and gains, and the circumstances in which financial assets and financial liabilities are offset. This new section will place

increased emphasis on disclosure regarding the nature and extent of risks arising from financial instruments and how the Corporation manages those risks. This Section applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. The Corporation is currently assessing the impact of the adoption of these standards on its consolidated financial statements.

In March 2007, the CICA issued Section 3862, "Financial Instruments – Disclosures", which replaces Section 3861 and provides expanded disclosure to enable users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. This standard harmonizes disclosures with International Financial Reporting Standards. This Section applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. The Corporation is currently assessing the impact of the adoption of these standards on its consolidated financial statements.

International Financial Reporting Standards

In May 2007, the CICA published an updated version of its "Implementation Plan for Incorporating International Financial Reporting Standards ("IFRS") into Canadian GAAP". This plan includes an outline of the key decisions that the CICA will need to make as it implements the Strategic Plan for publicly accountable enterprises that will converge Canadian generally accepted accounting principles with IFRS. The changeover date from Canadian GAAP to IFRS is for annual and interim financial statements relating to fiscal years beginning on or after January 1, 2011.

Goodwill and Intangible Assets

In February 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets", which replaces Section 3062, "Goodwill and Other Intangible Assets", and Section 3450, "Research and Development Costs". The purpose of this Section is to establish recognition, measurement, and disclosure of goodwill and intangible assets and to provide more specific guidance on the recognition of internally developed intangible assets and requires that research and development expenditures be evaluated against the same criteria as expenditures for intangible assets. The Section substantially harmonizes Canadian standards with International Financial Reporting Standards and applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008. It is not expected to have a material impact on the Corporation's consolidated financial statements.

Capital Disclosures

In December 2006, the CICA issued Section 1535, "Capital Disclosures", which establishes guidelines for the disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. Effective for fiscal periods beginning on or after October 1, 2007, this enhanced disclosure enables users to evaluate the entity's objectives, policies, and processes for managing capital. This new requirement is for disclosure only and will not impact the financial results of the Corporation.

4. RESTATEMENT OF PREVIOUSLY ISSUED FINANCIAL STATEMENTS

The Corporation is restating its previously reported consolidated financial statements for the fiscal year ended December 31, 2006. The following table summarizes the impact of the restatement adjustment on the previously reported consolidated balance sheet, income statement, and cash flow amounts for the year ended December 31, 2006

	2006 As Reported	Affecting Periods Prior to 2006	2006 Restatement	Ref	2006 As Restated
Balance Sheet Items					
Cash and cash equivalents	\$24,689,040	\$ —	\$(4,930,550)	a	\$ 19,758,490
Security deposits	—	—	1,220,209	a	1,220,209
Funds receivable from payment processors	—	—	3,710,341	a	3,710,341
Current portion of deferred costs	—	107,053	176,596	d	283,649
Current assets	29,124,218	107,053	176,596		29,407,867
<u>Goodwill</u>					
Public company costs		(50,000)		b	
Transition services costs		(671,653)	—	c	
Goodwill	4,850,722	(721,653)	—		4,129,069
Deferred costs	1,167,330	92,446	123,670	d	1,383,446
Total assets	40,652,942	(522,154)	300,266		40,431,054
Current portion of deferred revenue	158,788	222,048	395,415	d	776,251
Deferred revenue	—	238,257	184,219	d	422,476
Total liabilities	44,047,143	460,305	579,634		45,087,082
Deficit	(55,335,455)	(982,459)	(279,368)		(1,261,827)
Deficit - restated					(56,597,282)
Liabilities and Shareholders' Deficiency	\$40,652,942	\$ (522,154)	\$ 300,266		\$ 40,431,054

	2006 As Reported	2006 Restatement	Ref	2006 As Restated
Income Statement Items				
Total revenue	\$ 12,246,689	\$ (550,986)	d	\$ 11,695,703
Sales commission and related expenses	897,401	(79,214)	d	818,187
Employment costs	8,378,316	(221,052)	d	8,157,264
Foreign exchange loss (gain)	(19,329)	28,648	d	9,319
Net loss	\$ (7,906,695)	\$ (279,368)		\$ (8,186,063)
Loss per share	\$ (0.07)	\$ (0.01)		\$ (0.08)

(Expressed in Canadian Dollars)

	2006 As Reported	2006 Revised	2006 Restatement	Ref	2006 As Restated
Statement of Cash Flows					
Net Loss	\$ (7,906,695)		\$ (279,368)	d	\$ (8,186,063)
Items not affecting cash					
Unrealized foreign exchange loss / (gain)	2,189	208,558	(25,236)		185,511
Changes in non-cash balances related to operations					
Increase in security deposits			(245,421)	a	(245,421)
Increase in funds receivable from payment processors			(796,848)	a	(796,848)
Decrease in accounts receivable	489,817	126,094	–		615,911
Increase in deferred costs	–	–	(300,266)	d	(300,266)
Increase in prepaids and sundry assets	(218,064)	(184,791)	–		(402,855)
Increase (decrease) in accounts payable and accrued liabilities	1,018,764	(4)	–		1,018,760
Increase in deferred revenue		2,321	562,196	d	564,517
Increase (decrease) in payable to loyalty program partners	4,820,759	(40,499)	–		4,780,260
Changes in non cash balances related to operations	6,111,276	(96,879)	(780,339)		5,234,058
Cash flows provided by operating activities	3,002,907	111,679	(1,084,943)		2,029,643
Effect of exchange rate changes on Cash held in foreign currency	491,139	(111,679)	(91,870)	a	287,590
Increase in Cash and Cash Equivalents	4,705,433		(1,176,813)		3,528,620
Security deposits			(957,669)	a	
Funds receivable from payment processors	–		(2,796,068)	a	
Cash and Cash Equivalents - Beginning of year	19,983,607		(3,753,737)		16,229,870
Security deposits			(1,220,209)	a	
Funds receivable from payment processors			(3,710,341)	a	
Cash and Cash Equivalents - End of year	\$ 24,689,040		\$ (4,930,550)		\$ 19,758,490

The 2006 restated consolidated cash flow includes the impact of the restatements on the previously reported cash flow as well as some reclassifications made to the prior years reported amounts. These revisions incorporate the reclassification of certain items and corrections to an error in the prior years consolidated cash flow for the effect of exchange rate changes on cash held in foreign currency.

The summarized 2006 restatement adjustments set out above are a result of the specific restatement adjustments as follows:

(a) Restatement of Cash and Cash Equivalents, Security Deposits and Funds Receivable From Payment Processors:

Funds receivable from payment processors are amounts collected on behalf of the Corporation by payment processors. The funds are held for up to three days before being released to the Corporation. As such, these amounts do not meet the definition of cash and cash equivalents as previously reported and have been moved from cash and cash equivalents to funds receivable from payment processors. Security deposits are amounts held on a rolling six month basis by the Corporation's payment processors that process deposit and credit card transactions. Historically, these amounts were recorded as a component of cash and cash equivalents, with disclosure in the notes to the financial statements.

(b) Restatement of Public Company Costs:

In 2000, the Corporation became a public company through a reverse take over of its parent company. Costs of \$150,000 incurred to effect the reverse take over were incorrectly capitalized and included within Goodwill. This Goodwill item was subsequently amortized in 2000 and 2001, resulting in a carrying value of \$50,000 at the end of 2001. As a result of this restatement, the 2006 opening balance for Goodwill has been reduced by \$50,000 and the 2006 opening Deficit increased by the same amount.

The effect on 2006 opening balance is as follows:

Decrease in goodwill	(\$150,000)
Decrease in accumulated amortization of goodwill	\$100,000
Increase in deficit	(\$ 50,000)

(c) Restatement of Transition Services Costs in Goodwill:

Costs of \$365,515 and \$306,138 incurred in connection with the acquisition of the assets of Mile-Point, Inc. in 2004 and 2005, respectively, were incorrectly added to goodwill as they did not meet the definition of an acquisition cost as defined by CICA Handbook Section 1581 ("Business Combinations"). As these were integration and transition costs in nature, these costs should have been expensed as incurred. The financial statements of 2006 have been restated to correct these errors.

The effect on 2006 opening balance is as follows:

Decrease in goodwill	(\$671,653)
Increase in deficit	(\$671,653)

(d) Restatement of Upfront Contract Initiation Fees:

The Corporation has determined that it has contracts with multiple deliverables. As such, the Corporation has applied guidance found in Abstract 142 of the Emerging Issues Committee ("EIC-142") of the Canadian Institute of Chartered Accountants (CICA) Handbook, "Revenue Arrangements with Multiple Deliverables" and determined that, for some contracts, there was only one unit of accounting. In particular, for contracts which contain ongoing service requirements, fees and direct costs for initial set-up have been deferred and recognized evenly over the term of the contract. Previously, the fees and direct costs had incorrectly been recognized as initial set-up occurred. The impact of this correction is included below by year. The cumulative net effects of these errors prior to 2006 are recognized in the restated consolidated financial statements of 2006.

The effect is as follows:

	<u>2003-2005</u>	<u>2006</u>
Decrease in revenue as previously recognized	\$ (460,305)	\$ (550,986)
Decrease in costs as previously recognize	<u>199,499</u>	<u>271,618</u>
Decrease in net income	\$ (260,806)	\$ (279,368)
Increase in deferred revenue	\$ (460,305)	\$ (579,634)
Increase in deferred costs	<u>199,499</u>	<u>300,268</u>
Increase in deficit	\$ (260,806)	\$ (279,368)

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consists of:

	<u>2007</u>	<u>2006</u>
Cash	\$ 6,518,089	\$ 19,175,348
Term deposits	<u>14,630,242</u>	<u>583,142</u>
	<u>\$ 21,148,331</u>	<u>\$ 19,758,490</u>

6. FUNDS RECEIVABLE FROM PAYMENT PROCESSORS

Funds receivable from payment processors are funds due from the Corporation's credit card processors. These funds represent amounts collected from customers and are typically deposited directly to the Corporation's bank account within 3 business days from date of sale.

7. SHORT-TERM INVESTMENTS

As at December 31, 2007, the balance was comprised of \$7,174,000 (2006 – nil) in term deposits with maturity dates between 90 days and 12 months, and \$98,200 (2006 – nil) deposited with the Corporation's bank as collateral for a commercial letter of credit issued in accordance with the terms of a business arrangement. The interest rate on the short-term investments at year end was 5.31%.

8. SECURITY DEPOSITS

Security deposits are amounts held by the Corporation's payment processors as collateral in accordance with the terms of the credit card processing agreement. This collateral balance is based on a percentage of the Corporation's processing volume over a six month period.

9. ACCOUNTS RECEIVABLE

The Corporation's accounts receivable is comprised mainly of amounts owing to the Corporation by loyalty program partners for transactions carried out on the *Points.com* web site and for amounts charged with respect to the loyalty program sign-up and the technology design and development fees. The amount is presented net of an allowance for doubtful accounts. The allowance was \$72,401 at December 31, 2007 (December 31, 2006 - \$86,004).

10. PROPERTY AND EQUIPMENT

<u>2007</u>	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Furniture and equipment	\$ 533,433	\$ 335,276	\$ 198,157
Computer equipment	856,467	578,204	278,263
Software	1,351,850	1,151,085	200,766
Web site development & technology	8,327,234	7,232,865	1,094,369
Leasehold improvements	830,418	620,510	209,908
	<u>\$ 11,899,402</u>	<u>\$ 9,917,939</u>	<u>\$ 1,981,463</u>

<u>2006</u>	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Furniture and equipment	\$ 509,524	\$ 288,544	\$ 220,980
Computer equipment	745,273	483,208	262,065
Software	1,324,763	848,515	476,248
Web site development & technology	7,625,536	5,987,101	1,638,435
Leasehold improvements	829,298	492,787	336,511
	<u>\$ 11,034,394</u>	<u>\$ 8,100,155</u>	<u>\$ 2,934,239</u>

11. INTANGIBLE ASSETS AND GOODWILL

On March 31, 2004, the Corporation acquired substantially all of the business assets of MilePoint, Inc., a loyalty program technology provider and operator. As part of the acquisition, the Corporation acquired the customer list and all of the contracts between MilePoint and certain loyalty program partners for the operation of technology solutions. The fair values assigned were as follows:

Contracts with loyalty program partners	\$ 3,565,000
Customer list	225,000
Goodwill	4,129,069
Total	<u>\$ 7,919,069</u>

The Corporation had previously incorrectly included \$671,653 in transition service costs and \$50,000 of public listing costs in goodwill. These costs should have been expensed as incurred. The financial statements of 2006 have been restated to correct these errors. See notes 4 (b) and 4(c) for additional information. The MilePoint contracts are being amortized over the term of their life. The expected amortization over the next five years is as follows:

2008	\$ 125,212
2009	125,212
2010	125,212
2011	125,212
2012	20,867

Intangible Assets

Intangible assets of \$1,384,080 (2006 - \$1,986,433) is comprised of finite lived assets and indefinite lived assets.

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
<u>2007</u>			
Patents	\$ 788,478	\$ –	\$ 788,478
MilePoint contracts and customer list	<u>3,790,000</u>	<u>3,268,285</u>	<u>521,715</u>
	<u>\$ 4,578,478</u>	<u>\$ 3,268,285</u>	<u>\$ 1,310,193</u>
<u>2006</u>			
Patents	\$ 630,481	\$ –	\$ 630,481
MilePoint contracts and customer list	<u>3,790,000</u>	<u>2,507,789</u>	<u>1,282,211</u>
	<u>\$ 4,420,481</u>	<u>\$ 2,507,789</u>	<u>\$ 1,912,692</u>

a) Finite lived intangible assets

The Corporation has several patent applications pending approval in Australia, Canada and the United States that relate directly to the process and technology that run the current business platform. The carrying amounts are representative of actual costs incurred to date in pursuing patent applications. Patents will be amortized over the remaining life of the patent commencing when the patents have been granted. To date, none of the patents have been granted and therefore no amortization has been recorded.

For finite lived assets, the Corporation assesses impairment only if impairment indicators exist. If the carrying amount of the finite lived asset cannot be recovered from undiscounted cash flows, an appropriate amount will be charged to income as an “impairment charge” at that time.

b) Indefinite lived intangible assets

The Corporation holds several trademark registrations in Canada and the United States. The carrying amounts of \$73,887 (\$73,741 - December 31, 2006) are representative of actual costs incurred to date in registering trademarks. Registered trademarks have an indefinite life and will not be amortized unless it is determined that they have become impaired.

The Corporation tests its’ indefinite lived assets for impairment at least annually, to determine whether the carrying value exceeds the fair value. If it is determined that an impairment exists, it is recognized into net income at that time.

Goodwill – MilePoint acquisition

Goodwill of \$4,129,069 (2006 – \$4,129,069) relates entirely to the excess of the purchase price over the fair values of the business assets of MilePoint, Inc. acquired in 2004. In accordance with the CICA handbook Section 3062, “Goodwill and Other Intangible Assets”, a valuation of the goodwill occurs annually at year end. As at December 31, 2007, there has been no impairment.

12. DEFERRED COSTS

Deferred costs include deferred financing charges, direct costs associated with securing key relationships with loyalty program partners and the direct costs associated with the web site application development in relation to the

Corporation's technology design and development revenues involving revenue arrangements with multiple deliverables.

<u>Upfront contract initiation costs</u>	<u>2007</u>	<u>2006</u>
Current	\$ 274,327	\$ 283,649
Long term	148,593	216,116
Total	<u>\$ 422,920</u>	<u>\$ 499,765</u>

Deferred finance charges for the Series Two Preferred Share represent legal, accounting and other related fees incurred to obtain the financing; these costs are amortized over the term of the financing and were included in deferred costs at December 31, 2006. Effective January 1, 2007, the company adopted Section 3855 ("Financial Instruments – Recognition and Measurement"), which require that the transaction costs associated with a financing be included in the carrying value of the financial instrument.

Direct costs associated with securing key loyalty program partner relationships and in relation to the Corporations partner sign-up and technology design and development revenues are deferred over the expected life of the agreement.

<u>2007</u>	<u>Cost</u>	<u>Accumulated Ammortization</u>	<u>Net Carrying Amount</u>
Partnership relationship costs	2,363,958	2,037,578	326,380
	<u>\$ 2,363,958</u>	<u>\$ 2,037,578</u>	<u>\$ 326,380</u>

<u>2006</u>	<u>Cost</u>	<u>Accumulated Ammortization</u>	<u>Net Carrying Amount</u>
Series Two Preferred Share and Warrants	589,050	220,894	368,156
Partner relationship costs	2,363,958	1,564,784	799,174
	<u>\$ 2,953,008</u>	<u>\$ 1,785,678</u>	<u>\$ 1,167,330</u>

As part of securing the relationship with one of the Corporation's key loyalty program partners, the Corporation issued shares to the loyalty program partner. The value of these shares is being amortized over the expected benefit period of this relationship.

<u>Non- Current Deferred Costs</u>	<u>2007</u>	<u>2006</u>
Upfront contract initiation costs	148,593	216,116
Partner Relationships & Series Two Preferred Shares	<u>326,380</u>	<u>1,167,330</u>
Total	<u>\$ 474,973</u>	<u>\$ 1,383,446</u>

13. LOAN PAYABLE

In August of 2004, the Corporation entered into an agreement with its landlord, whereby the landlord loaned the Corporation \$107,000 in respect of amounts that the Corporation had spent on leasehold improvements. The loan is repayable over 43 months and bears an interest rate of 10%. There are 2 months remaining as at December 31, 2007.

14. CONVERTIBLE DEBENTURES

On April 11, 2006, the common share purchase warrant held by an affiliate of IAC/InterActiveCorp, which was exercisable to acquire approximately 103 million common shares, expired unexercised. As a result, the Corporation's 8% unsecured convertible debentures ("Debentures") automatically converted at the agreed upon conversion price of \$0.3173 per common share as specified in the Debentures into approximately 18.9 million common shares and the \$9.9 million of principal and accrued interest on the Debentures was converted to equity. The conversion price of the Debentures was determined to be \$6.0 million based on the agreed upon conversion price of \$0.3173 per common share as specified in the Debentures agreement.

The impact on the financial statements of the expiry of the IAC/InterActiveCorp warrant was to increase contributed surplus and to decrease warrants by \$2,572,000 (the fair value of the warrant). The expiry had no impact on shareholder's deficiency. As at April 12th, 2006, the Debentures converted into equity. The impact was a reduction of \$9.9 million in long term liabilities and the \$6.0 million value (as determined by the agreed upon conversion price) assigned to the 18.9 million common shares issued, was recorded as an increase to share capital. The difference between the Debentures amount of \$9.9 million and the \$6.0 million recorded as share capital was credited to contributed surplus.

15. CONVERTIBLE PREFERRED SHARES

a) Series One Preferred Share

On April 11, 2006, the common share purchase warrant held by an affiliate of IAC/InterActiveCorp, which was exercisable to acquire approximately 103 million common shares, expired unexercised. As a result, the Corporation's Series One Preferred Share automatically converted into one common share, eliminating the significant dividend entitlement that would have been payable to the holders of the Series One Preferred Share in certain events, including a change of control of the Corporation.

b) Series Two Preferred Share

In 2003, the Corporation issued one Series Two Preferred Share for aggregate consideration of \$12.4 million. The Series Two Preferred Share is a voting, convertible share and ranks equally with the Series One Preferred Share, the Series Three Preferred Share, the Series Four Preferred Share and the Series Five Preferred Share, and in priority to the Common Shares. The Series Two Preferred Share is convertible until 5:00 p.m. on March 31, 2013 (Toronto time), for no additional consideration, into 24,028,016 common shares subject to adjustment in accordance with its anti-dilution protection provisions (the "Underlying Shares").

The Corporation is not entitled to declare or pay any dividend on the common shares unless it concurrently declares and pays a dividend on the Series Two Preferred Share in an amount equal to the product of the number of common shares comprising the Underlying Shares and the dividend declared or paid per common share. Any such dividend is to be paid to the holder of the Series Two Preferred Share in the same form as it is paid to the holders of the common shares.

The Series Two Preferred Share will automatically convert into one Series Three Preferred Share on the earlier of the date that (i) the Series Two Preferred Share is directly or indirectly transferred to a person that is not an affiliate of IAC/InterActiveCorp, and (ii) the holder of the Series Two Preferred Share ceases to be an affiliate of IAC/InterActiveCorp.

If not converted, the Series Two Preferred Share will be redeemed on March 31, 2013 for the greater of \$12,400,000 plus 7% per annum calculated on a daily basis from the date of issue of the Series Two Preferred Share to the date on which the Series Two Preferred Share is redeemed and the market value of the common shares into which the Series Two Preferred Share then could be converted. As of December 31, 2007, the carrying value of the Series Two Preferred Share is \$16,187,226 (\$15,628,478 at December 31, 2006). Non cash interest expense recorded in connection with the Series Two Preferred

Share was \$926,905 (2006 - \$1,109,823). Effective January 1, 2007, the company adopted Section 3855 ("Financial Instruments – Recognition and Measurement"), which requires that the transaction costs associated with a financing be included in the carrying value of the financial instrument. The adoption of this standard resulted in a reduction of \$368,157 to the opening balance of the Series Two Preferred Share.

In the event of the liquidation, dissolution or winding-up of the Corporation or other distribution of assets of the Corporation among its shareholders for the purpose of winding up its affairs, the holder of the Series Two Preferred Share will be entitled to receive from the assets of the Corporation an amount equal to the greater of (i) \$12,400,000 plus 7% per annum calculated on a daily basis from the date of issue of the Series Two Preferred Share to the date on which the liquidation event occurred and (ii) the product of the number of Underlying Shares and the per share amount to be distributed to the holders of the common shares upon the liquidation event after giving effect to any payments to be paid on the Series Two Preferred Share and any other shares (other than the Series Two Preferred Share) ranking in priority to the common shares upon the liquidation event.

The Series Two Preferred Share entitles the holder to the right to vote with the holders of common shares on an "as converted" basis to a maximum of 19.9% of the votes that may be cast), vote separately as a series with respect to certain material transactions and certain other matters involving the Corporation, and elect two members to the board of directors of the Corporation and have one member sit on each committee of the board of directors.

c) **Series Three Preferred Share**

The Series Three Preferred Share is a non-voting, non-convertible share ranking equally with the Series Two Preferred Share, the Series Four Preferred Share and the Series Five Preferred Share, and in priority to the Common Shares. The Series Three Preferred Share is not entitled to receive dividends. If issued, the Corporation will redeem the Series Three Preferred Share on March 31, 2013. In the event of redemption on March 31, 2013, the amount payable will be equal to \$12,400,000 plus 7% per annum from the date of issue of the Series Two Preferred Share. In the event of redemption following a specified change of control event, the amount payable will be equal to 125% of the amount specified in the preceding sentence.

In the event of the liquidation, dissolution or winding up of the Corporation, whether voluntary or involuntary, the holder of the Series Three Preferred Share will be entitled to receive from the assets of the Corporation an amount equal to \$12,400,000 plus 7% per annum, calculated from the date of issue of the Series Two Preferred Share to the date on which the liquidation event occurred.

No Series Three Preferred Shares are outstanding.

d) **Series Four Preferred Share**

In 2005, the Corporation issued one Series Four Preferred Share for aggregate cash consideration of \$3,454,611.

The Series Four Preferred Share is a voting, convertible share and ranks equally with the Series One Preferred Share, the Series Two Preferred Share, the Series Three Preferred Share and the Series Five Preferred Share, and in priority to the Common Shares. The Series Four Preferred Share is convertible until 5:00 p.m. on March 31, 2013 (Toronto time), for no additional consideration, into 5,411,434 common shares, subject to adjustment in accordance with its anti-dilution protection provisions. In all material respects, including anti-dilution protection, the terms of the Series Four Preferred Share are identical to the Series Two Preferred Share.

If not converted, the Series Four Preferred Share will be redeemed by the Corporation on March 31, 2013 for the greater of \$3,454,611 plus 7% per annum calculated on a daily basis from the date of issue of the

Series Four Preferred Share and the market value of the common shares into which the Series Four Preferred Share then could be converted. As of December 31, 2007, the carrying value of the Series Four Preferred Share is \$4,119,624 (\$3,877,801 at December 31, 2006). Non cash interest expense recorded in connection with the Series Four Preferred Share was \$241,823 (2006 - \$241,823).

In the event of the liquidation, dissolution or winding-up of the Corporation, the holder of the Series Four Preferred Share will be entitled to receive an amount equal to the greater of \$3,454,611 plus 7% per annum from the date of issuance and the product of the number of common shares into which it could then be converted and the per share amount to be distributed to the holders of the common shares after giving effect to any payments to be paid on shares ranking in priority to the common shares.

The Series Four Preferred Share entitles the holder to various rights, including to receive dividends with the holders of common shares on an "as converted" basis, vote with the holders of common shares on an "as converted" basis (in certain circumstances, to a maximum of 19.9% of the votes that may be cast including the votes cast by the holder of the Series Two Preferred Share), vote separately as a series with respect to certain material transactions and certain other matters involving the Corporation, and elect one member to the board of directors of the Corporation. If the Series Four Preferred Share ceases to be held by an IAC/InterActiveCorp or an affiliate of IAC/InterActiveCorp, it will automatically convert into a Series Five Preferred Share.

e) **Series Five Preferred Share**

The Series Five Preferred Share is a non-voting, non-convertible share ranking equally with the Series Two Preferred Share, Series Three Preferred Share and Series Four Preferred Share, and in priority to the Common Shares. The Series Five Preferred Share is not entitled to receive dividends. If issued, the Corporation will redeem the Series Five Preferred Share on March 31, 2013. In the event of redemption on March 31, 2013, the amount payable will equal \$3,454,611 plus 7% per annum from the date of issuance of the Series Four Preferred Share. In the event of redemption following a specified change of control event, the amount payable will be equal to 125% of the amount specified in the preceding sentence.

In the event of the liquidation, dissolution or winding up of the Corporation, whether voluntary or involuntary, the holder of the Series Five Preferred Share will be entitled to receive from the assets of the Corporation an amount equal to \$3,454,611 plus 7% per annum, calculated from the date of issue of the Series Four Preferred Share to the date on which the liquidation event occurred.

No Series Five Preferred Shares are outstanding.

16. CAPITAL STOCK

Authorized Unlimited	Common Shares
	1 Series Two Preferred Share
	1 Series Three Preferred Share
	1 Series Four Preferred Share
	1 Series Five Preferred Share
Issued	

The balance of capital stock is summarized as follows:

<u>Common Shares</u>	<u>Number</u>	<u>Cash Proceeds</u>	<u>Amount</u>
Balance January 1, 2006	93,717,709		\$ 36,404,34
Issued on exercise of stock options (i)	890,840	\$ 422,785	450,720
Issued in exchange for property (shares in subsidiary) (ii)	687,570	15,104	195,987
Other common shares (iii)	<u>18,908,070</u>	<u>—</u>	<u>6,000,000</u>
Balance December 31, 2006	114,204,189	\$ 437,887	\$ 43,051,048
Issued on exercise of stock options (iv)	1,224,434	760,042	1,076,639
Issued in exchange for property (shares in subsidiary) (v)	3,834,114	56,606	1,081,828
Issued on exercise of warrants (vi)	<u>757,378</u>	<u>628,624</u>	<u>784,644</u>
Balance December 31, 2007	<u>120,020,115</u>	<u>\$ 1,445,272</u>	<u>\$45,994,159</u>

- i) 890,840 options previously issued to employees, directors, advisors and consultants were exercised at prices ranging from \$0.20 to \$0.60 per share.
- ii) 274,600 options previously issued to Points.com Inc. founders, employees, directors and advisors were exercised in Points.com Inc. and put to the Corporation at fair market value for 687,570 of the Corporation's common shares.
- iii) On April 11, 2006 Convertible Debentures were automatically converted to 18,908,070 common shares and the series one preferred share converted to 1 common share.
- iv) 1,224,434 options previously issued to employees, directors, advisors and consultants were exercised at prices ranging from \$0.22 to \$1.37 per share.
- v) 1,531,257 options previously issued to Points.com Inc. founders, employees, directors and advisors were exercised in Points.com Inc. and put to the Corporation at fair market value for 3,834,114 of the Corporation's common shares.
- vi) 757,378 common share purchase warrants (valued at \$156,020), issued in connection with the IAC/InterActiveCorp financing, were exercised for consideration of \$628,624.

17. OPTIONS AND WARRANTS

a) Stock option plan

The Corporation has a stock option plan under which employees, directors and consultants are periodically granted stock options to purchase common shares at prices not less than the market price of the common shares on the day prior to the date of grant. The options generally vest over a three year period and expire five years from the grant date. The 2007 exceptions to the three-year vesting period consist of 100,000 options which vested upon grant and 600,000 options which vest based on performance criteria and expire five years from the grant date.

	<u>2007</u>	<u>2006</u>
Options Authorized by Shareholders	14,058,406	14,058,406
Less: Options Exercised	<u>(6,599,813)</u>	<u>(5,375,379)</u>
Net Options Authorized	7,458,593	8,683,02
Less: Options Issued & Outstanding	<u>(7,202,541)</u>	<u>(4,113,085)</u>
Options Available to Grant	<u>256,052</u>	<u>4,569,942</u>

b) Stock options

Stock-based compensation plan

At December 31, 2007, the Corporation had one stock-based compensation plan, which is described above. The Corporation accounts for stock options granted under this plan in accordance with the fair-value based method of accounting for stock-based compensation. The estimated fair value of the options that are ultimately expected to vest is recorded over the option's vesting period and charged to stock-based compensation. In determining the amount of options that are expected to vest, the Corporation takes into account voluntary termination behaviour as well as trends of actual option forfeitures. The compensation cost that has been charged against income and included in employment costs for this plan is \$583,934 for 2007 (\$366,981 for 2006).

Fair value

The fair value of each option grant is estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in years 2003 to 2007 respectively: dividend yield of nil for all five years; expected volatility is calculated for each grant date and has ranged from 29% to 91%, risk-free interest rate has ranged from 3.5% to 4.5% with an expected life of 3.0 years.

	<u>2007</u>	<u>2006</u>
Dividend yield	nil	nil
Risk free rate	4.07%	4.05%
Expected volatility	42.1%	40.1%
Expected life of options	3	3

A summary of the status of the Corporation's stock option plan as of December 31, 2007 and 2006, and changes during the years ended on those dates is presented below.

	<u>2007</u>		<u>2006</u>	
	Number of <u>options</u>	Weighted average <u>exercise price</u>	Number of <u>options</u>	Weighted average <u>exercise</u>
Beginning of Year	4,113,085	\$ 0.86	4,866,913	\$ 0.83
Granted	5,177,334	1.26	1,377,500	0.82
Exercised	(1,224,434)	0.62	(890,840)	0.47
Forfeited	(863,444)	1.01	(1,240,488)	0.97
End of year	<u>7,202,541</u>	<u>\$ 1.17</u>	<u>4,113,085</u>	<u>\$ 0.86</u>
Exercisable at end of year	<u>1,624,499</u>	<u>\$ 1.00</u>	<u>2,778,181</u>	<u>\$ 0.84</u>
Weighted average fair value of options granted		<u>\$ 0.28</u>		<u>\$ 0.43</u>

	<u>Options outstanding</u>			<u>Options exercisable</u>		
	Number of <u>options</u>	Weighted average remaining contractual <u>life (years)</u>	Weighted average <u>exercise price</u>	Number of <u>Options</u>	Weighted average <u>exercise price</u>	
\$0.01 to \$0.49	65,000	0.13	\$ 0.22	65,000	\$ 0.22	
\$0.50 to \$0.99	2,008,667	3.42	0.84	553,125	0.80	
\$1.00 to \$1.49	3,830,874	43	1.16	1,006,374	1.16	
\$1.50 to \$1.99	1,248,000	4.38	1.77	0	n/a	
\$2.00 and over	<u>50,000</u>	4.78	2.02	<u>0</u>	n/a	
	<u>7,202,541</u>			<u>1,634,499</u>		

Options outstanding but not yet exercisable:

	<u>Vest based on employee service</u>		<u>Vest based on performance critieria</u>	
<u>Range of Exercise Price</u>	Number of <u>Options</u>	Weighted average <u>exercise price</u>	Number of <u>options</u>	Weighted average <u>exercise price</u>
\$0.01 to \$0.49	–	n/a	–	n/a
\$0.50 to \$0.99	1,455,542	\$ 0.85	–	n/a
\$1.00 to \$1.49	2,224,500	1.15	600,000	\$ 1.23
\$1.50 to \$1.99	1,248,000	1.77	–	n/a
\$2.00 and over	<u>50,000</u>	2.02	<u>–</u>	n/a
	<u>4,978,042</u>		<u>600,000</u>	

Options issued in 2007:

	<u>Exercise price equals market price on grant</u>		<u>Exercise price exceeds market price on grant</u>	
<u>Range of Exercise Price</u>	Number of <u>Options</u>	Weighted average <u>exercise price</u>	Number of <u>options</u>	Weighted average <u>exercise price</u>
\$0.01 to \$0.49	–	n/a	–	n/a
\$0.50 to \$0.99	1,207,334	\$ 0.90	–	n/a
\$1.00 to \$1.49	1,400,000	1.08	1,267,000	\$ 1.28
\$1.50 to \$1.99	420,000	1.71	833,000	1.80
\$2.00 and over	<u>50,000</u>	2.02	<u>–</u>	n/a
	<u>3,077,334</u>		<u>2,100,000</u>	

The expense to be recognized in future periods from the options outstanding at year-end is \$1,211,062. Subsequent to year-end, 140,815 options were exercised, 35,000 options were granted and none were cancelled.

c) Stock options of Points.com Inc.

In addition to the stock options described above, Points.com Inc., the Corporation's indirect wholly owned subsidiary had one stock compensation plan. No further Points.com Inc. common shares are authorized for issuance under this plan and all previously outstanding options have been exercised. Under this plan, Points.com Inc. founders, employees, directors and advisors were previously issued and, therefore, had outstanding stock options. No options were granted in this plan subsequent to 2000. The options outstanding are as follows:

	<u>2007</u>		<u>2006</u>	
	Number of <u>options</u>	Weighted average <u>exercise price</u>	Number of <u>options</u>	Weighted average <u>exercise price</u>
Beginning of Year	1,531,257	\$ 0.03	1,805,857	\$ 0.04
Granted	—	—	—	—
Exercised	(1,531,257)	0.03	(274,600)	0.06
Forfeited	—	—	—	—
End of year	<u>—</u>	<u>—</u>	<u>1,531,257</u>	<u>\$ 0.03</u>
Exercisable at end of year	<u>—</u>	<u>—</u>	<u>1,531,257</u>	<u>\$ 0.03</u>

The holders of 1,531,257 options (all with strike prices at or below \$0.055 per share) had the right to put to the Corporation the common shares of Points.com Inc. acquired on the exercise of such options for common shares in the Corporation. The Corporation used a ratio of 2.5039 common shares per Points.com Inc. common share for this purpose. In 2007, all remaining 1,531,257 options were exercised and all of the Points.com Inc. common shares received were put to the Corporation for 3,834,114 common shares of the Corporation.

d) Warrants

On April 11, 2006, the common share purchase warrant held by an affiliate of IAC/InterActiveCorp, which was exercisable to acquire approximately 103 million common shares, expired unexercised. As a result, the Corporation's 8% unsecured convertible debentures ("Debentures"), which had a face value of \$6.0 million, were automatically converted into approximately 18.9 million common shares using the conversion price of \$0.3173 per common share as specified in the Debentures. The \$9.9 million carrying value of the Debentures (principal and accrued interest) has been converted to equity.

Also as a result, the Corporation's Series One Preferred Share automatically converted into one common share, eliminating the significant dividend entitlement that would have been payable to the holders of the Series One Preferred Share in certain events, including a change of control of the Corporation.

The impact on the financial statements of the expiry of the IAC/InterActiveCorp warrant was to increase contributed surplus and to decrease warrants for \$2,572,000 (the fair value of the warrant). The expiry has no impact on shareholder's equity. As at April 12th, 2006, the Debentures converted to equity. The impact is a reduction of \$9.9 million in long term liabilities and the \$6.0 million value (as determined by the agreed upon conversion price) assigned to the 18.9 million common shares issued, has been recorded as an increase to share capital. The difference between the Debentures amount of \$9.9 million and the \$6.0 million recorded as share capital has been credited to contributed surplus.

	<u>2007</u>		<u>2006</u>	
	Number of <u>warrants</u>	Weighted average <u>exercise price</u>	Number of <u>Warrants</u>	Weighted average <u>exercise price</u>
Beginning of Year	906,248	\$ 0.83	103,529,530	\$ 0.93
Granted	—	—	—	—
Exercised	(757,378)	0.83	—	—
Forfeited	—	—	(102,623,282)	0.93
End of year	<u>148,870</u>	<u>0.83</u>	<u>906,248</u>	<u>0.83</u>
Exercisable at end of year	<u>148,870</u>	<u>0.83</u>	<u>906,248</u>	<u>0.83</u>

Range of exercise price	Warrants outstanding			Warrants exercisable	
	Number of warrants	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of warrants	Weighted average exercise price
\$0.01 to \$0.49	–	–	–	–	–
\$0.50 to \$0.99	148,870	0.26	\$ 0.83	148,870	\$0.83
\$1.00 and over	–	–	–	–	–

e) Warrants of Points.com Inc.

Points.com Inc., had issued or committed to issue 2,848,050 warrants to airline loyalty program partners that expired unexercised on April 1, 2007. Each warrant entitled the holder to acquire one common share of Points.com Inc. with an exercise price of US\$1.96.

f) Fair Value

The weighted average grant date fair value of warrants granted were estimated at their grant date at \$0.21 using the Black Scholes option pricing model. The pricing model assumed a weighted average risk free interest rates of 3.8%, weighted average expected dividend yields of nil, weighted average expected common stock price volatility of 30% and a weighted average expected life of 3 years. During the year, 757,378 common share purchase warrants (valued at \$156,020), issued in connection with the IAC/InterActiveCorp financing, were exercised for consideration of \$628,624.

g) Contributed Surplus

The changes in contributed surplus are as follows:

	<u>2007</u>	<u>2006</u>
Contributed Surplus – opening balance	\$ 8,703,518	\$ 2,079,423
Compensation cost	583,934	366,980
Fair value of options exercised	(1,341,819)	(208,819)
Fair value of expired warrant (Note 14)	–	2,572,000
Convertible debenture conversion into equity (Note 14)	–	3,893,934
Contributed Surplus – ending balance	<u>\$ 7,945,633</u>	<u>\$ 8,703,518</u>

18. OPERATING EXPENSES

Operating expenses are comprised of:

	<u>2007</u>	<u>2006</u>
Office expenses, travel and personnel	\$ 1,365,295	\$ 1,143,585
Professional fees	1,147,488	827,770
Insurance, bad debts and governance	646,231	768,172
	<u>\$ 3,159,014</u>	<u>\$ 2,739,528</u>

19. LOSS PER SHARE

a) Loss per share

Loss per share is calculated on the basis of the weighted average number of common shares outstanding for the year that amounted to 118,307,829 shares (2006 – 108,258,453).

b) Diluted loss per share

The diluted loss per share is equal to basic loss per share as the effect of conversions, options and warrants would be anti dilutive.

20. STATEMENT OF CASH FLOWS

a) Changes in non cash balances related to operations are as follows:

	<u>2007</u>	<u>2006</u>
(Increase) in security deposits	\$ (562,818)	\$ (245,421)
(Increase) in funds receivable from payment processors	(1,835,560)	(796,848)
(Increase) decrease in accounts receivable	(1,351,431)	615,911
(Increase) decrease in deferred costs	76,844	(300,266)
Decrease (increase) in prepaids and sundry assets	7,964	(402,855)
Increase in accounts payable and accrued liabilities	391,350	1,018,760
Increase in deferred revenue	990,610	564,517
Increase in payable to loyalty program partners	<u>13,414,361</u>	<u>4,780,260</u>
	<u>\$ 11,131,320</u>	<u>\$ 5,234,058</u>

b) Supplemental information

Interest and taxes

Interest of \$4,421 (2006 \$20,341) was paid during the year. In addition to this, the Corporation paid capital taxes of \$40,279 (2006 - \$37,113) in the year. Interest revenue of \$676,488 (2006 \$218,667) was received during the year.

Non cash transactions in 2007 were as follows:

For the years ended December 31	2007	2006
Options exercised in Points.com Inc.		
Number of options (Note 17(c))	1,531,257	274,600
Common shares issued of Points International Ltd.	3,834,114	687,570
Fair value	\$1,025,222	180,883
Loyalty currency received as a reimbursement (i)	-	184,552
Revenue earned for membership fees paid in one week accommodation certificates (ii)	37,322	146,322
Revenue earned for sign-up fees paid in research services for <i>Points.com</i> web site (iii)	-	50,000
Revenue earned for hosting services paid in loyalty currency (iv)	-	17,008

- (i) The currency is included in prepaid and sundry assets and the cost is recognized as the currency is used.
- (ii) The certificates are valued at their average cost and are included in prepaid and sundry assets. The cost is recognized as the accommodation certificates are used.
- (iii) The research services are valued at their market value and are included in prepaid and sundry assets. The cost is recognized as the services are used.
- (iv) The loyalty currency was valued at the purchase price of the miles and the amount included in prepaid and sundry assets.

21. FINANCIAL INSTRUMENTS

The fair values of short term financial assets and liabilities, including cash, short term deposits, interest receivable and accounts payable and accrued liabilities, as presented in the balance sheet approximate their carrying amounts due to the short period to maturity of these financial instruments.

The carrying value and estimated fair value of the Corporation's financial instruments is their fair value which is the amount that has been recorded in the financial statements.

The Corporation has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies, as disclosed below. However, considerable judgment can be required to develop certain of these estimates. Accordingly, these estimated values are not necessarily indicative of the amounts the Corporation could realize in a current market exchange. The estimated fair value amounts can be materially affected by the use of different assumptions or methodologies. The methods and assumptions used to estimate the fair value of each class of financial instruments are discussed below.

Fair value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value is determined by reference to quoted bid or ask prices, as appropriate, in the most advantageous active market for that instrument to which the Corporation has immediate access. When bid and ask prices are unavailable, the Corporation uses the closing price of the most recent transaction of that instrument. In the absence of an active market, the Corporation would determine fair value based on internal or external valuation models, such as option-pricing models, and discounted cash flow analysis, using observable market-based inputs.

Credit risk

The Corporation's cash and cash equivalents subject the Corporation to credit risk. The Corporation has guaranteed investment certificates, as per its practice of protecting its capital rather than maximizing investment yield. The Corporation manages credit risk by investing in cash equivalents, term deposits and short term investments rated as A or R1 or above.

The Corporation, in the normal course of business, is exposed to credit risk from its customers and the accounts receivable are subject to normal industry risks. The Corporation attempts to manage these risks by dealing with credit-worthy customers.

Interest rate risk

The Corporation does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates, relative to interest rates on the investments, owing to the short term nature of the investments. Interest rates, maturities and security affecting the currency, interest and credit risk of the Corporation's financial assets and liabilities have been disclosed in Note 2 (p).

Currency risk

The Corporation has customers and suppliers that are not based in Canada which gives rise to a risk that earnings and cash flows may be adversely affected by fluctuations in foreign currency exchange rates. The Corporation is primarily exposed to the US dollar. The Corporation currently does not use financial instruments to hedge these risks.

(Expressed in Canadian Dollars)

Balances denominated in foreign currencies that are considered financial instruments are as follows:

As of December 31, 2007	CAD\$ Total	US\$	GBP	EUR	CHF
FX Rates used to translate to CAD		\$ 0.982	1.96	1.4464	0.872
Financial assets (in thousands of dollars)					
Cash and cash equivalents	\$ 21,148	16,391	1,056	1,483	22
Funds receivable from payment processor	5,034	3,932	325	359	4
Short term investments	7,272	7,100	–	–	–
Security deposits	1,533	1,394	24	74	–
Accounts receivable	3,293	2,785	27	15	–
Total	\$ 38,280	US\$31,602	GBP 1,432	EUR 1,931	CHF 26
Financial liabilities					
Accounts payable and accrued liabilities	\$ 3,425	1,448	8	–	–
Payable to loyalty program partners	30,196	26,593	1,011	1,444	11
Convertible Preferred Shares	20,307	–	–	–	–
Total	\$ 53,928	US\$ 28,041	GBP 1,019	EUR 1,444	CHF 11

22. INCOME TAXES

The total provision for income taxes differs from that amount which would be computed by applying the Canadian federal income tax rate to the loss before provision for income taxes. The reasons for these differences are as follows:

	<u>2007</u>	<u>2006</u>
Income tax recovery at statutory rate of 36.12%	\$ (1,602,000)	\$ (2,856,000)
Increase (decrease) in income taxes resulting from:		
Lower effective income tax rates in foreign jurisdictions	20,000	–
Lower effective income tax rate on future taxes	51,000	–
Tax cost of non-deductible items	816,000	12,000
Losses for which no benefit has been recorded	715,000	1,774,000
Change in valuation allowance	–	1,070,000
Actual income tax expense (recovery)	<u>\$ –</u>	<u>\$ –</u>

The Corporation has non capital losses carry forward for income tax purposes in the amount of approximately \$33,792,000 which may be applied against future years' taxable income. The losses may be used to reduce future years' taxable income and expire approximately as follows:

Year	Total CAD	Jurisdiction		
		Canada	United Kingdom	United States
2008	\$ 6,035,000	\$ 6,035,000	\$ –	\$ –
2009	5,917,000	5,917,000	–	–
2010	3,597,000	3,597,000	–	–
2011	5,427,000	5,427,000	–	–
2015	5,596,000	5,596,000	–	–
2022-2025	781,000	–	–	781,000
2026	3,629,000	3,292,000	–	337,000
2027	1,838,000	1,714,000	–	124,000
No expiry	<u>972,000</u>	<u>–</u>	<u>972,000</u>	<u>–</u>
Total	\$ 33,792,000	\$ 31,578,000	\$ 972,000	\$ 1,242,000

The nature and tax effects of the items that give rise to significant portions of the future income tax assets and future income tax liabilities are as follows:

Future income tax assets are comprised of:	<u>2007</u>	<u>2006</u>
Losses carried forward	\$ 9,853,000	\$ 13,230,000
Property and equipment	2,662,000	2,647,000
Share issue costs	<u>189,000</u>	<u>1,156,000</u>
	12,704,000	17,033,000
Valuation allowance	<u>(12,114,000)</u>	<u>(16,443,000)</u>
Net future income tax asset	<u>\$ 590,000</u>	<u>\$ 590,000</u>

23. RELATED PARTY TRANSACTIONS

The following are the transactions and balances with related parties:

In fiscal 2007 and 2006, certain officers and directors exercised stock options in the Corporation and the Corporation's subsidiary Points.com Inc. (Note 16 (ii) and Note 16 (v)). These transactions were part of the normal course of business and have been recorded at the exchange amount. There are no amounts receivable or payable from these transactions.

24. COMMITMENTS

The Corporation is obligated under various operating leases for premises, purchase commitments and equipment and service agreements for web hosting services expiring through 2012 to aggregate annual rentals as follows:

2008	\$ 1,773,503
2009	993,604
2010	613,149
2011	21,347
2012	14,040

In relation to principal revenue, the Corporation has made contractual guarantees on the minimum value of transactions processed over the term of its agreements with certain loyalty program partners. These guarantees have a maximum potential value by fiscal year as follows and have not been recognized in the financial statements:

2008	\$ 1,506,429
2009	5,962,885
2010	6,206,289

25. SEGMENTED INFORMATION

a) Reportable segments

The Corporation has only one operating segment, the portfolio of technology solutions to the loyalty program industry in each of 2007 and 2006 whose operating results were regularly reviewed by the Corporation's chief operating decision maker and for which complete and discrete financial information is available.

b) Enterprise wide disclosures - Geographic information

\$30,102,199 (2006 \$10,327,127), representing 95% of the Corporation's revenue, was generated in the U.S., \$374,863 (2006 - \$414,647), representing 1%, was generated in Canada and the remaining revenue was generated outside North America.

At December 31, 2007 and 2006, substantially all of the Corporation's assets were in Canada.

26. MAJOR CUSTOMERS

For the year ended December 31, 2007, there were three customers who individually represented more than 10% of the Corporation's total revenue. In aggregate these three customers represented 75% (three customers in 2006 represented 58%) of the Corporation's total revenue. In addition, 65% (2006 - 65%) of the Corporation's amount Payable to loyalty program partners are due to these three customers.

27. COMPARATIVE FIGURES

Certain comparative figures have been reclassified in accordance with the current year's presentation.

28. UNITED STATES GAAP ("US GAAP") RECONCILIATION
Canadian and United States Accounting Policy Differences

The consolidated financial statements of the Corporation have been prepared in accordance with Canadian GAAP. The significant differences between Canadian GAAP and US GAAP, and their effect on the consolidated financial statements of the Corporation, are described below.

Consolidated statements of operations:

The following table reconciles net loss as reported in the accompanying consolidated statements of loss to net loss that would have been reported had the financial statements been prepared in accordance with US GAAP:

	Years ended December 31	
	<u>2007</u>	<u>2006 - Restated</u>
Net loss in accordance with Canadian GAAP	\$ (4,436,335)	\$ (8,186,063)
Web site development amortization (a)	<u>98,528</u>	<u>98,528</u>
Net loss in accordance with US GAAP	<u>\$ (4,337,807)</u>	<u>\$ (8,087,535)</u>
Loss per share	<u>\$ (0.04)</u>	<u>\$ (0.07)</u>

The cumulative effect of these adjustments on shareholders' deficiency is as follows:

	As at December 31	
	<u>2007</u>	<u>2006 - Restated</u>
Shareholders' deficiency in accordance with Canadian GAAP	\$ (7,063,157)	\$ (4,656,028)
Web site development (a)	(819,400)	(819,400)
Web site development amortization (a)	<u>794,767</u>	<u>696,239</u>
Shareholders' deficiency in accordance with US GAAP	<u>\$ (7,087,790)</u>	<u>\$ (4,779,189)</u>

The cumulative effect of these adjustments on the Corporation's reported assets is as follows:

	As at December 31	
	2007	2006 - Restated
Assets in accordance with Canadian GAAP	\$ 48,850,568	\$ 40,431,054
Web site Development Costs (a)	(819,400)	(819,400)
Web site Development Amortization (a)	<u>794,7676</u>	<u>96,239</u>
Assets in accordance with US GAAP	<u>\$ 48,825,935</u>	<u>\$ 40,307,893</u>

There is no difference in cash flows under US GAAP.

a) Web Site Development Costs

Canadian GAAP allows the capitalization and amortization of web site development costs incurred, subject to there being reasonable assurance that future benefits will be realized. Under US GAAP, American Institute of Certified Public Accountants, Statement of Position "SOP" 98-1 provides specific guidance on when capitalization may commence, and what direct costs may be capitalized. For US GAAP purposes, costs incurred in the preliminary project phase have been expensed at the time the costs were incurred and the amortization recorded under Canadian GAAP would have been reversed.

Restatement or Previously Issued Financial Statements

The US GAAP reconciliation has been reconciled to give effect to the restatement adjustment in the Corporation's previously issued financial statements. The Canadian GAAP results have been restated and this has resulted in a decrease of \$221,888 from \$40,652,942 in the Corporation's total assets at the end of 2006 and an increase in the shareholder's deficiency of \$1,261,827 from a negative \$55,335,455. The net loss for the year ended has increased by \$279,368 from a previously reported \$7,906,695 to a restated net loss of \$8,186,063.

Guidance for Quantifying Financial Statement Misstatements

In September 2006, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ("SAB 108"). SEC staff issued SAB 108 to address what they identified as diversity in practice whereby entities were using either an income statement approach or a balance sheet approach, but not both, when evaluating whether an error is material to an entity's financial statements. SAB 108 requires that in quantifying and analyzing misstatements, both the income statement approach and the balance sheet approach should be used to evaluate the materiality of financial statement misstatements. SAB 108 became effective for the Corporation commencing with the year ended December 31, 2006.

Accounting for Uncertainty in Income Taxes

In June 2006, the FASB issued FIN 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes" ("SFAS 109"). The interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides accounting guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The evaluation of tax positions under FIN 48 is a two-step process, whereby (1) Points determines whether it is more likely than not that the tax positions will be sustained based on the technical merits of the position and (2) for those tax positions that meet the more-likely-than-not recognition threshold, the Corporation would recognize the largest amount of tax benefit that is greater than fifty percent likely of being realized upon ultimate settlement with

the related tax authority. The Corporation has not adopted FIN 48 for Canadian GAAP purposes. Based on the Corporation's assessment, the adoption of FIN 48 had no impact on its statement of position or results of operations, prepared in accordance with U.S. GAAP

Impact of Accounting Pronouncements Not Yet Adopted

Fair Value Measurements

In September 2006, the FASB issued SFAS 157 Fair Value Measurements. SFAS 157 clarifies the definition of fair value, establishes a framework for measurement of fair value, and expands disclosure about fair value measurements. SFAS 157 is effective for fiscal years beginning after December 15, 2007 and the Corporation will be required to adopt the standard in the first quarter of fiscal 2008. The Corporation is currently evaluating what impact, if any, SFAS 157 will have on its consolidated financial statements.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS 159 The Fair Value Option for Financial Assets and Financial Liabilities -Including an Amendment of SFAS 115. SFAS 159 permits entities to measure many financial instruments and certain other items at fair value that currently are not required to be measured at fair value. If elected, unrealized gains or losses on certain items will be reported in earnings at each subsequent reporting period. SFAS 159 is effective for the Corporation as of the beginning of its 2008 fiscal year. The Corporation has not determined whether it will elect to adopt the fair value measurement provisions of this statement, or what impact it will have on its consolidated financial statements.

Business Combinations

In December 2007, the FASB issued SFAS 141(R) Business Combinations. SFAS 141(R) replaces SFAS 141 Business Combinations. SFAS 141(R) is broader in scope than SFAS 141 which applied only to business combinations in which control was obtained by transferring consideration. SFAS 141(R) applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008 and the Company will be required to adopt the standard in the first quarter of fiscal 2009. The Company has not determined what impact SFAS 141(R) will have on its consolidated financial statements.

Noncontrolling Interests in Consolidated Financial Statements

In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 160 ("FAS 160"), Noncontrolling Interests in Consolidated Financial Statements, which establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. FAS 160 is effective for financial statements issued for fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. The Company presently does not expect FAS 160 to have an effect on its financial statements.