

CONSOLIDATED BALANCE SHEETS

(stated in thousands of dollars) (unaudited)

	June 30, 2010	December 31, 2009
ASSETS		
Current		
Cash and cash equivalents	\$ 883	\$ 460
Accounts receivable (note 3)	16,041	16,156
Inventory	217	199
Prepaid expenses and other assets	1,439	1,654
Income taxes recoverable	1,095	398
	<u>19,675</u>	<u>18,867</u>
Property and equipment	26,906	28,595
Intangible assets	2,996	3,260
	<u>\$ 49,577</u>	<u>\$ 50,722</u>
LIABILITIES		
Current		
Accounts payable and accrued liabilities	\$ 5,496	\$ 4,667
Income taxes payable	84	72
Current portion of obligation under capital leases	170	233
Current portion of long-term debt (note 4)	2,114	5,222
Current portion of deferred gain	137	137
	<u>8,001</u>	<u>10,331</u>
Deferred gain	250	319
Obligations under capital leases	43	122
Long-term debt (note 4)	3,611	818
Future income taxes	4,035	4,170
	<u>15,940</u>	<u>15,760</u>
SHAREHOLDERS' EQUITY		
Share capital (note 5)	60,040	60,040
Contributed surplus	4,850	4,755
Deficit	(31,213)	(29,770)
Accumulated other comprehensive income (loss)	(40)	(63)
	<u>33,637</u>	<u>34,962</u>
	<u>\$ 49,577</u>	<u>\$ 50,722</u>
Contingencies (note 7)		

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF LOSS

(stated in thousands of dollars) (unaudited)	Three months ended June 30		Six months ended June 30	
	2010	2009	2010	2009
REVENUE	\$ 18,350	19,566	\$ 39,257	41,967
COSTS				
Operating and materials	16,825	18,145	34,551	38,555
Selling, general and administrative	1,905	1,872	3,864	4,079
Amortization of property and equipment	1,264	1,554	2,702	3,165
Amortization of intangible assets	132	138	264	266
Stock-based compensation	87	99	128	149
Interest on long-term debt	101	103	184	234
Other interest and bank charges	39	17	74	35
Foreign exchange (gain) loss	(1)	12	(6)	11
(Gain) loss on disposal of property and equipment	(218)	126	(605)	219
	20,134	22,066	41,156	46,713
LOSS BEFORE INCOME TAX	(1,784)	(2,500)	(1,899)	(4,746)
Income taxes				
Current recovery	(505)	-	(314)	-
Future reduction	(44)	(572)	(142)	(1,012)
	(549)	(572)	(456)	(1,012)
NET LOSS	\$ (1,235)	(1,928)	\$ (1,443)	(3,734)
Loss per share				
Basic and diluted	\$ (0.03)	(0.05)	\$ (0.04)	(0.10)
Weighted average shares outstanding				
Basic	37,576	37,576	37,576	37,576
Diluted	37,576	37,576	37,576	37,576

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(stated in thousands of dollars) (unaudited)	Three months ended June 30		Six months ended June 30	
	2010	2009	2010	2009
Net Loss	\$ (1,235)	(1,928)	\$ (1,443)	(3,734)
Unrealized gain (loss) on translating financial statement of self-sustaining foreign operations	58	(43)	23	(85)
Comprehensive loss	\$ (1,177)	(1,971)	\$ (1,420)	(3,819)

CONSOLIDATED STATEMENTS OF DEFICIT AND ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

(stated in thousands of dollars) (unaudited)	Three months ended June 30		Six months ended June 30	
	2010	2009	2010	2009
Deficit, beginning of period	\$ (29,978)	(24,942)	\$ (29,770)	(23,136)
Net loss	(1,235)	(1,928)	(1,443)	(3,734)
Deficit, end of period	\$ (31,213)	(26,870)	\$ (31,213)	(26,870)
Accumulated other comprehensive income (loss), beginning of period	\$ (98)	82	\$ (63)	124
Unrealized gain (loss) on translating financial statements of self-sustaining foreign operations	58	(43)	23	(85)
Accumulated other comprehensive income (loss), end of period	\$ (40)	39	\$ (40)	39

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(stated in thousands of dollars) (unaudited)	Three months ended June 30		Six months ended June 30	
	2010	2009	2010	2009
Cash provided by Operations				
Net loss	\$ (1,235)	(1,928)	\$ (1,443)	(3,734)
Charges to income not involving cash:				
Amortization	1,396	1,692	2,966	3,431
Stock-based compensation	87	99	128	149
Future income tax reduction	(44)	(572)	(142)	(1,012)
(Gain) loss on disposal of property and equipment	(218)	126	(605)	219
Change in non-cash working capital (note 9)	1,627	5,932	439	6,877
Cash provided by operations	1,613	5,349	1,343	5,930
Financing				
Repayment of obligations under capital leases	(70)	(318)	(143)	(669)
Non-revolving term loan facility	5,000	-	5,000	-
Repayment of long-term debt	(5,370)	(67)	(5,333)	(104)
Amortization of deferred financing fees	19	-	19	-
Cash used in financing activities	(421)	(385)	(457)	(773)
Investing				
Purchase of property and equipment	(520)	(437)	(1,037)	(901)
Proceeds from disposal of property and equipment	133	312	575	521
Cash used in investing activities	(387)	(125)	(462)	(380)
Cash flow from operating, financing and investing activities	805	4,839	424	4,777
Effect of exchange rate on foreign currency held	8	23	(1)	32
Net change in cash and cash equivalents	813	4,862	423	4,809
Cash and cash equivalents, beginning of period	70	1,061	460	1,114
Cash and cash equivalents, end of period	\$ 883	5,923	\$ 883	5,923

See accompanying notes to the consolidated financial statements.

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Notes to the Consolidated Financial Statements
For the three and six month periods ended June 30, 2010 and 2009
(stated in thousands of dollars) (unaudited)

NOTE 1 – BASIS OF PRESENTATION

These unaudited interim consolidated financial statements of HSE Integrated Ltd. (“HSE” or “the Company”) have been prepared following the same accounting policies and methods of computation as the audited annual consolidated financial statements of the Company for the year ended December 31, 2009. The disclosures provided below are incremental to those included with the audited annual consolidated financial statements and certain disclosures which are normally required to be included in the notes to the annual consolidated financial statements have been condensed or omitted. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes for the Company for the year ended December 31, 2009.

These unaudited interim consolidated financial statements include the accounts of the Company and its subsidiaries which, with the exception of Boots & Coots HSE Services LLC (note 8), are wholly owned. Unless otherwise specified all amounts are stated in thousands of Canadian dollars except for per-share amounts, which are stated in dollars per weighted-average share.

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). In preparing these consolidated financial statements, management is required to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from these estimates.

HSE’s business has two offsetting seasonal components. Revenue for Oilfield health and safety services is historically highest in the first and fourth quarters and lowest in the second quarter because this sector uses equipment that can only access well locations during certain times of the year and because of the effects of weather on field activity. Industrial revenue includes a mix of year-round contracts and “turnarounds” – scheduled major maintenance projects and repair activities on client facilities. These turnarounds tend to be scheduled during the second and third quarters to avoid the possibility of adverse effects from freezing weather. As a result, Industrial revenue tends to be highest in the second and third quarters.

NOTE 2 – CHANGE IN ACCOUNTING STANDARDS

Accounting Standards Pending Adoption

Business Combinations, Consolidated Financial Statements and Non-controlling Interests

In January 2009, the AcSB issued three new recommendations regarding business combinations, consolidated financial statements and non-controlling interests. While these standards are effective for fiscal years beginning on or after January 1, 2011, early adoption is permitted if all three standards are adopted simultaneously. The new standards include:

- Section 1582, which will replace Section 1581, deals with accounting for business combinations. The new standard harmonizes Canadian accounting standards with IFRS 3 – Business Combinations. Section 1582 is applicable prospectively to business combinations entered into after adoption.
- Sections 1601 and 1602 together will replace existing section 1600. Section 1601 provides standards for the preparation of consolidated financial statements, while section 1602 provides standards with respect to accounting for non-controlling interests in subsidiaries. The new standard harmonizes Canadian accounting standards with proposed revisions to IAS 27 – Consolidated and Separate Financial Statements. It makes changes to the circumstances under which the Company must consolidate an entity, as well as to disclosure requirements.

The impact of these standards on the Company’s financial statements will depend upon the timing and nature of any future acquisitions.

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Notes to the Consolidated Financial Statements
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NOTE 3 – FINANCIAL RISK MANAGEMENT**Overview**

The Company is exposed to the following risks from its financial instruments:

- credit risk
- liquidity risk
- market risk

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk-management framework. The Company's Audit Committee oversees how management monitors compliance with the Company's risk-management practices and reviews the adequacy of the risk-management framework in relation to the risks faced by the Company. The Company's risk-management practices are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers.

The Company's accounts receivable are due from customers in a variety of industries including a significant proportion with customers operating in the energy and manufacturing industries. The ability of customers within the energy industry to pay us is partially affected by fluctuations in the price they receive for various hydrocarbon products. The maximum credit exposure associated with trade accounts receivable is the carrying value.

The Company follows a credit policy under which the Company reviews each new customer individually for credit worthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes external ratings, where available, and trade references. Customers that fail to meet the Company's credit worthiness criteria may transact with the Company only on a prepayment basis. On an ongoing basis, the Company also reviews the payment patterns of its existing customers and the customers' continued credit worthiness.

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company determines the allowance by reviewing individual accounts past due for collectability, historical write-off experience, and overall account aging. The Company reviews its allowance for doubtful accounts on an ongoing basis, but at least monthly.

	June 30, 2010		December 31, 2009	
Trade accounts receivable	\$	17,282	\$	17,416
Allowance for doubtful accounts		(1,241)		(1,260)
Total trade accounts receivable	\$	16,041	\$	16,156

The aging of trade receivables from the invoice date is as follows:

	June 30, 2010				December 31, 2009	
	Gross		Allowance		Gross	Allowance
Past due:						
0 – 30 days (current)	\$	10,590	\$	–	\$	7,938
31 – 60 days		2,733		–		5,135
61 – 120 days		3,247		529		3,433
More than 120 days		712		712		910
Total	\$	17,282	\$	1,241	\$	17,416
					\$	1,260

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Notes to the Consolidated Financial Statements
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NOTE 3 – FINANCIAL RISK MANAGEMENT (CONTINUED)

The movement in the allowance for doubtful accounts receivables in respect of trade receivables during the period is as follows:

	2010	2009
Balance, April 1	\$ 1,255	\$ 1,490
Bad-debt provision	–	106
Write-offs net of recoveries	(14)	(386)
Balance, June 30	\$ 1,241	\$ 1,210

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company requires liquidity to meet financial obligations as they come due and to fund our investing activities.

The Company's contractual financial liabilities include interest payments, trade and other payables, income taxes payable, a revolving operating line of credit margined to accounts receivable and property and equipment and capital leases for equipment (note 4).

The Company's approach to managing liquidity is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and distressed conditions, without unacceptable losses or risking damage to the Company's reputation. The Company generally relies on operating cash flow to provide liquidity to meet its financial obligations. As well, the Company had access to undrawn operating lines of credit of \$10.0 million and cash on hand of \$0.9 million at June 30, 2010.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Company's income.

HSE is exposed to currency risk on U.S.-dollar denominated financial assets and liabilities. The Company adjusts the reported amounts of foreign-currency denominated financial assets and liabilities to their Canadian-dollar equivalent at each balance sheet date. For amounts held directly by the Company, any related foreign exchange gains and/or losses are recognized in the consolidated statement of earnings. For amounts held by the Company's self-sustaining foreign operations, the amount is included in other comprehensive income. At June 30, 2010, the extent of this exposure was not material.

HSE is exposed to interest rate risk on its prime-based revolving operating facility. Based on amounts outstanding at June 30, 2010, a 1% increase in the average prime interest rate for the year would cost the Company \$45 annually in additional interest expense.

NOTE 4 – OPERATING FACILITIES AND LONG-TERM DEBT

On April 27, 2010 the Company entered into a \$15,000 credit facility with a regional financial institution. The facility consists of a \$10,000 operating revolving loan facility for general operating purposes and a \$5,000 non-revolving reducing loan facility. The two facilities were used to retire the \$5,300 existing bank debt.

The \$5,000 non-revolving term facility is repayable in monthly payments of \$109 starting July 1, 2010. The facility is payable in full 48 months after initial drawdown. The operating facility is renewable annually and is margined to accounts receivable. Both facilities bear interest at prime plus a fixed percentage. A standby fee is also required on any unused portion of the operating facility. Both facilities are subject to certain covenants including a working capital covenant, a debt to equity covenant, a fixed charge coverage ratio and other positive and negative covenants. The facilities are collateralized under a general security agreement and include accounts receivable and property and equipment.

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NOTE 4 – OPERATING FACILITIES AND LONG-TERM DEBT (CONTINUED)

As at June 30, 2010, the Company was in default of the fixed charge coverage covenant which gave the regional financial institution the right to demand immediate repayment of the loan facility. The default was remedied with a covenant waiver received August 4, 2010, prior to the financial statements being completed. The financial institution waived the covenant for the periods June 30, September 30 and December 31, 2010 conditional upon the Company being compliant with all covenants on March 31, 2011. As at June 30, 2010, the total outstanding on the loan facility was \$5,000 of which \$1,304 was current. The fixed charge coverage covenant is the ratio of earnings before interest, taxes, depreciation and amortization less capital expenditures to interest and principal repayments.

Deferred financing costs associated with the financing facilities have been shown as a reduction in the carrying value of the long-term debt and are being expensed over the term of the debt based on the effective interest rate method.

	June 30 2010	December 31 2009
Equipment financing contracts	\$ -	\$ 33
Non-revolving term loan facility	5,000	5,300
	5,000	5,333
Accrued consideration on share-purchase acquisition	810	810
	5,810	6,143
Less unamortized debt-issue costs	(85)	(103)
Less current portion	(2,114)	(5,222)
	\$ 3,611	\$ 818

Outstanding principal repayments are due as follows:

Years ended June 30	
2011	\$ 2,114
2012	1,304
2013	1,304
2014	1,088
	5,810
Less: current portion and unamortized debt-issue costs	(2,199)
	\$ 3,611

NOTE 5 – SHARE CAPITAL AND STOCK-BASED COMPENSATION PLANS

At June 30, 2010 there were 37,575,675 common shares of the Company outstanding (December 31, 2009 – 37,575,675).

At June 30, 2010, the Company had options outstanding to issue 2,577,497 shares (December 31, 2009 – 2,375,333) at a weighted average price of \$1.34 per share (December 31, 2009 – \$1.56). Of these options, 1,536,142 were exercisable (December 31, 2009 – 1,360,315).

Incentive stock option plan

The weighted average fair value of options issued for the quarter ended June 30, 2010 was \$0.38 (2009 – \$0.26). The fair value of each option granted was estimated on the date of grant using the Merton Black-Scholes option-pricing model with the following assumptions:

	June 30, 2010	December 31, 2009
Vesting period (years)	3	3
Risk-free interest rate	2.60%	1.69%
Expected life (years)	5	5
Price volatility	100.74%	92.78%

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NOTE 5 – SHARE CAPITAL AND STOCK-BASED COMPENSATION PLANS (CONTINUED)

Pursuant to the stock-option plan, a maximum of 10% of the issued and outstanding common shares of the Company are reserved from time to time for issuance to eligible participants. The directors determine option prices and vesting terms at the time of granting at an exercise price based on the volume weighted average price for the five trading days immediately preceding the grant date. The term of options granted does not exceed five years.

Information about outstanding stock options is as follows:

	June 30, 2010		December 31, 2009	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding, beginning of year	2,375,333	\$ 1.56	2,533,499	\$ 1.88
Granted	715,000	0.49	650,000	0.36
Exercised	–	–	–	–
Forfeited	(512,836)	1.14	(808,166)	1.62
Outstanding, end of period	2,577,497	\$ 1.34	2,375,333	\$ 1.56
Exercisable at end of period	1,536,142	\$ 1.91	1,360,315	\$ 2.18

The following table summarizes information about stock options outstanding at June 30, 2010:

Options Outstanding	Exercise Prices (\$)	Weighted Average Remaining Life	Number Exercisable
1,534,164	0.25 - 1.19	3.92	494,142
427,833	1.20 - 2.14	1.62	426,500
245,500	2.15 - 3.09	0.60	245,500
370,000	3.10 - 4.04	0.78	370,000
2,577,497	1.34	2.77	1,536,142

Deferred share unit plan

For the 2010 and 2009 years, the directors' retainers and meeting fees are being paid with deferred share units (DSU's). The total DSU's outstanding at June 30, 2010 were 325,601. On April 5, 2010, 103,263 DSU's were granted and on May 21, 2010 an additional 26,896 DSU's were granted. The units are re-valued quarterly and any change in value is included as an increase or decrease in stock based compensation expense and accrued liabilities. The expense recognized for the quarter ended June 30, 2010 was \$41 (quarter ended June 30, 2009 - \$43)

NOTE 6 – RELATED-PARTY TRANSACTIONS

During the quarter, the Company had the following transactions with related parties, all of which are measured at exchange amounts.

- In the second quarter, the Company paid rent and property taxes of \$105 (2009 – \$103) for a regional office to a corporation related to a Director of the Company.
- In the second quarter, the Company also paid rent of \$78 (2009 – \$74) for a regional office to a corporation controlled by a Senior Manager of the Company.
- In the second quarter, the Company paid \$85 (2009 - \$0) for supplies and commissions to a corporation related to a Director of the Company pursuant to the terms of an agreement that pre-dates the directorship.

NOTE 7 – CONTINGENCIES

HSE Integrated Ltd.

Notes to the Consolidated Financial Statements
For the three and six month periods ended June 30, 2010 and 2009
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In the ordinary course of business activities, the Company may be contingently liable for litigation and claims with customers, suppliers, former employees, and third parties. Management believes that adequate provisions have been recorded in the accounts where applicable. Although it may not be possible to estimate accurately the extent of potential costs and losses, if any, management believes that the ultimate resolution of such contingencies would not have a material effect on the financial position of the Company.

NOTE 8 – SEGMENT INFORMATION

The Company operates in two main geographic areas: Canada and the United States (U.S.). Each geographic area has a President responsible for the operations and strategy of his area's business. Personnel working within a particular region report to the President, and the President reports to the Chief Executive Officer.

Within each geographic segment, the Company uses common resources to provide services to a variety of customer industries. The Company groups these customer industries into two categories. "Oilfield" services are provided to customers in the conventional upstream, or "wellhead", sector of the oil and gas industry. "Industrial" services are provided to customers in a variety of other industries including: non-conventional upstream oil development and production (including oilsands extraction); oil and gas processing; petrochemicals; pulp and paper; utilities; power generation; and manufacturing. It also includes worker safety training and safety management services.

Corporate division expenses consist of salary expenses, stock compensation, and office costs related to corporate employees, as well as public company costs.

For the three months ended June 30, 2010, no one customer provided more than 10% of the Company's revenue (June 30, 2009 – one customer). During the three months ended June 30, 2009, the Company had sales of approximately 2.4 million to this customer.

On May 7, 2008, a new company called Boots & Coots HSE Services LLC ("BCHSE") was incorporated to pursue the expansion of Oilfield safety services in the continental United States. The Company owns 100% of the shares of HSE Integrated Inc. ("INC") a Delaware corporation that in turn owns a 90% interest in BCHSE, a Delaware Limited Liability Company. Boots & Coots Services, Inc. owns the remaining 10% interest. A non-controlling interest has not been recorded as BCHSE has incurred losses to date.

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NOTE 8 – SEGMENT INFORMATION (CONTINUED)

	Three months ended June 30							
	Canada		U.S.		Corporate		Total	
	2010	2009	2010	2009	2010	2009	2010	2009
Revenue								
Oilfield	\$ 6,027	\$ 4,226	397	91	-	-	\$ 6,424	\$ 4,317
Industrial	11,435	15,130	491	119	-	-	11,926	15,249
Total revenue	\$17,462	\$19,356	\$ 888	\$ 210	-	-	\$18,350	\$19,566
Operating income (loss) ⁽¹⁾	1,260	1,671	265	(250)	(1,905)	(1,872)	(380)	(451)
Interest expense	-	-	-	-	140	120	140	120
Amortization of property and equipment and intangibles	1,372	1,669	24	23	-	-	1,396	1,692
Property and equipment	25,616	31,829	1,290	1,213	-	-	26,906	33,042
Intangibles	2,996	3,522	-	-	-	-	2,996	3,522
Capital expenditures ⁽²⁾	316	402	204	35	-	-	520	437

(1) Operating income (loss) is defined as net income (loss) before amortization of property and equipment and intangibles, interest, foreign exchange gains or losses, gains or losses on disposal of capital assets, share-based compensation, and income taxes.

(2) Property and equipment for Corporate is included in Canada

	Six months ended June 30							
	Canada		U.S.		Corporate		Total	
	2010	2009	2010	2009	2010	2009	2010	2009
Revenue								
Oilfield	\$14,821	\$14,468	\$ 586	\$ 109	-	-	\$15,407	\$14,577
Industrial	22,951	26,998	899	392	-	-	23,850	27,390
Total revenue	\$37,772	\$41,466	\$ 1,485	\$ 501	-	-	\$39,257	\$41,967
Operating income (loss) ⁽¹⁾	4,395	4,024	311	(612)	(3,864)	(4,079)	842	(667)
Interest expense	-	-	-	-	258	269	258	269
Amortization of property and equipment and intangibles	2,919	3,388	47	43	-	-	2,966	3,431
Property and equipment	25,616	31,829	1,290	1,213	-	-	26,906	33,042
Intangibles	2,996	3,522	-	-	-	-	2,996	3,522
Capital expenditures ^{(2),(3)}	774	615	263	286	-	-	1,037	901

(1) Operating income (loss) is defined as net income (loss) before amortization of property and equipment and intangibles, interest, foreign exchange gains or losses, gains or losses on disposal of capital assets, share-based compensation, and income taxes.

(2) Property and equipment for Corporate is included in Canada

(3) \$197 in property and equipment was transferred from Canada to the U.S. year-to-date June 30, 2009

HSE Integrated Ltd.

Notes to the Consolidated Financial Statements
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(stated in thousands of dollars) (unaudited)

NOTE 9 – SUPPLEMENTARY CASH FLOW INFORMATION

	Three months ended June 30		Six months ended June 30	
	2010	2009	2010	2009
Changes in non-cash working capital from operations:				
Accounts receivable	\$ 2,183	6,795	\$ 135	9,084
Inventory	(4)	(8)	(18)	(19)
Prepaid expenses and other assets	181	143	222	552
Accounts payable and accrued liabilities	125	(995)	784	(2,978)
Income tax payable (recoverable)	(858)	(3)	(684)	238
Net change	\$ 1,627	5,932	\$ 439	6,877